

**Management Control Systems in a Transition  
Context: Case Studies from the Libyan Industrial  
Sector**

**MUSA ABOTWERAT RAMADAN OMAR**

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**Heriot-Watt University**

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## Abstract

This research study is the first attempt to explore and understand management control systems in the Libyan developmental context. The focus of this study is to explore and understand the actual situation of the MCSs in a number of Libyan industrial companies during their transition from the public sector to the private one by using the interpretive approach, systems ideas and case studies as the main research strategy. A theoretical framework based on systems ideas has guided this researcher to explore particular propositions (or focuses about which propositions are tentatively made) in the empirical work.

The study brings out that the Libyan transition context, involving change in ownership of organisations in the public sector with their transfer to the private sector, presents a unique situation for the implementation of management control systems. There is a change not just in the ownership of these organisations but also a change ostensibly sought in organisational objectives (towards profit-making). The study also brought out that, in the context of this change, management control systems such as the accounting system, cost and pricing system and budget system have been changing in terms of functioning and perceptions. The study finds that changes to accounting systems and the functioning of accounting systems in the privatised factories were constrained *vis-à-vis* the pursuit of the ostensible objectives by many environmental factors such as state intervention, economic sanctions, political policy and cultural manifestations. These factors have problematically affected in various ways aspects of the management control systems in these privatised organisations. Accounting's role is variously constrained and problematic (in relation, for instance, to the setting and achieving of goals and decision-making) and the trajectory of its functioning in the dynamic context has engendered some problematic and unanticipated consequences *vis-à-vis* the ostensible objectives involved.



# Chapter 1: Introduction

## 1.0 Research area and problem

Recently, management control systems (hereafter, MCSs) have become one of the central concerns of development theory and practice. Hopper and Powell (1985), Otley, (1989) and Hoque *et al.* (1994) concluded that in the context of development there is a need for better management control, so that management becomes more efficient and effective. Generally speaking, it could be argued that every country would benefit from its organisations having more effective and efficient systems to provide the necessary information for decision-makers in the context of planning and control.

One of the systems that plays a vital role in improving the quality of development plans and decision making is the accounting control system. One should emphasise here that management accounting is very important to the kind of dynamic and innovative enterprises that might be expected in a development context to aid them in the monitoring and control of their activities (Mitchell and Reid, 2000). Macintosh and Daft (1983, p.49) stated that “a management accounting system is one element in a package of control systems”.

In this respect, much has been written in western literature about accounting in developed countries and their environments, but relatively little has been written by local writers about accounting in developing nations and equally little has been written that has focused in depth upon specific nations in this context. As a result of this shortage of knowledge about the accounting situation in particular nations, it was felt that intensive research was needed to explore and understand accounting in a Libyan context. To date, it appears that no study focusing on MCSs in the Libyan selected industries within their developmental environment has been conducted. It should be noted that the empirical dimension of this research will be conducted in an environment that is different from a Western environment in order to explore and understand the



influence of different environmental factors on the MCSs. Ryan *et al.* (1992) also reflect the view that management accounting practices are not so much natural as decidedly social phenomena. They are socially structured and can be substantively changed according to the will and interaction of social actors.

Management control is an area of study that can be considered to be a broadening out of management accounting. Academics and researchers have defined management control in a number of different ways. For instance, for Sizer (1979): “Control is concerned not with correcting past mistakes, but directing future activities. Thus management control consists, in part, of inducing people in an organisation to do certain things and to refrain from doing others”. Anthony and Govindarajan (1998, p.6) defined management control as “the process by which managers influence other members of the organisation to implement the organisation’s strategies”. Beer (1959) described management as the profession of control, stating that the vital function and purpose of having managers in an organisation is to ensure that all activities are managed in a manner that will achieve the desired outcomes of the enterprise.

For Anthony (1965), the essence of managerial work is that it seeks to monitor and control individual activities and to co-ordinate them in such a way that they achieve their general purposes: management control is conventionally regarded as a set of practices designed to ensure that individuals, organisations and societies satisfy their goals. Also, Bhadada (1986) stated that management control is the part of the management process through which a manager ensures that the results of operations under his/her supervision conform as closely as possible to established goals. Lowe and Chua (1983, p.286), broadening matters out somewhat, noted that management control “is concerned with ensuring the achievement of a negotiated level of welfare for any organisation and its contributors consistent with maintaining boundary conditions for that enterprise, in relation to its environment.” Lowe and Chua (1983) also suggest that “organisational effectiveness be defined in terms of survival of the whole [organisation] in the long run where survival is indicative of the satisfactory fulfilment of member needs”. According to this definition, an effective organisation is one that satisfies a specific set of demands.



In terms of management control attainment, Berry *et al.* (1998) argued that the control process could be achieved by a set of interrelated units contracting with each other. According to Berry *et al.*, the control system has at least four devices to accomplish its mission in an organisation; a detector to discover what is happening; a selector to assess the actual situation; an effector for corrective actions; and a communication network to transmit information. By these means, managers can ensure that the organisation goes where they want it to go. Berry *et al.* (1998, p.18) also suggested that the MCS is “a system [that] consists of a structure and a process; that is, what it is and what it does.” The structure of an MCS can be described in terms of the units in an organisation and the nature of the information that flows among these units; the process is what the managers do with this information.

The discussion so far is based on definitions and studies that were conducted on specific companies and in a specific context (the Western environment), which might reflect a quite narrow rather than more holistic understanding of accounting. In this thesis, the aim is to leave the Western environment and cross over the Mediterranean Sea (a different context, see Chapter 4) in order to achieve a broader and contextual understanding of accounting and control, with the focus on MCSs in the dynamic context of Libya.

Management control is a field that has been widely examined, although relatively rarely in the context of its environment (Greenhalgh, 2000). This thesis attempts to understand the relationships between socio-political and economic factors and the organisational processes of MCSs in the Libyan industrial sector. Hoque *et al.* (1994, p.432) support the aim of understanding the relationship between an organisation and its environment as follows: “An organisation cannot be divorced from politics and the environment in which it operates, whatever its organisational structure.” An understanding of the MCSs within the social and organisational context is required so as to understand more adequately the interaction between the organisation and its environment. Boland and Pondy (1983, p.223) wrote that research on accounting in its organisational context “is most fruitfully done by attempting to understand how its rational and natural aspects



interact within the lived experience of individuals.” Otley and Berry (1994, p.46) also stated that “the role of accounting and other controls cannot be fully understood in isolation, and that a more contextual approach is required.” As a result of different environments, MCSs in general and the accounting system in particular can be practised and designed in a number of different ways. Indeed, Mueller (1967) noted that the existing accounting rules in a country are the product of economic, political and other environmental factors, which determine the nature of the system.

Understanding monitoring and control systems of enterprises with the focus on specific environment greatly aids an understanding of organisational ability to develop and achieve plans and goals. This is supported by the work of Drury and Tayles (1995) who stated that during the past decade there has been an increase in the perception of the importance and an increase of emphasis on the study of management accounting practices within their organisational context. In addition, Macintosh and Daft (1987) argued that the reason that there is still not a good understanding of how management accounting systems (hereafter, MASs) function is that the role of the MAS in organisational control has traditionally been studied in isolation from the characteristics of the total organisation and from other control systems. In order to broaden our understanding of MCSs within their environment, systems ideas are seen as appropriate (Lowe, 1972; Lowe and Tinker, 1977; Otley, 1989; Puxty, 1993), the elements of understanding thereby offered being developed through an interpretive approach to research study (see Burrell and Morgan, 1979; Chua, 1988; Puxty, 1993). A combination between systems ideas and an interpretive approach is understood to achieve this research interest. It can engender an holistic understanding of existing MCSs. It can be informed by being close to participants in order to understand the phenomena under study from their words and experience.

To sum up: the area of this research is management control and the focus of this thesis is to explore and understand the actual situation of the MCSs in certain Libyan ‘private’ organisations, to understand the environmental factors that are influencing and shaping these systems in the Libyan developmental context and also to understand the general



interaction between these MCSs and their context by application of systems ideas within an interpretive framework.

## **1.1 Research motivations and research significance**

### **1.1.1 The research interest**

The main objective of the research of this thesis is to attempt to gain a better understanding of the ways in which people manage and control their activities in specific organisations in the Libyan industrial sector within the context of the Libyan developmental environment. Through a multiple case study approach, this research attempts to achieve this objective by focusing on industrial enterprises in the Libyan Food, Paper and Construction Materials sectors. These enterprises have, ostensibly, had their ownership transferred from the public to private sector with the aim of promoting greater self-sufficiency in basic products for Libyan society. Otley and Berry (1980) suggested that studying the ways in which an organisation manages and controls its affairs by also identifying the relationships between socio-economic and political factors and the organisational processes of such MCSs to achieve its desired objectives has received little attention. This suggestion still has some validity in developing countries in general and in Libya in particular. Arriving at an understanding of the existing MCSs with regard to the transition of public enterprises to private ones and the effects of the contextual factors on these systems in the case study enterprises, within the Libyan socio-economic and political context, is one of the aims of this research. It is consistent with the research interest to explore and understand the actual situation of the MCSs and the relationships between these systems and their environment in the period of transition from public to private sector.

The principal aims of this research can be summarised as follows:

- to explore and gain an in-depth understanding of the MCSs and the accounting systems integrated thereto in the developmental context of transition in Libya, implicating privatisation, to understand the systems that have been mobilised in

this context, and the rationales for them, in the cases chosen from the Libyan private sector;

- to thus identify and elaborate the contextual factors influencing the implementation and operation of MCSs in the dynamic context and to elaborate the general organisation-environment interaction as an aspect of MCSs in this transition period;
- to tentatively assess the trajectory of these developments, including against the ostensible objectives involved;
- to provide a sense of the issues managers of the Libyan firms face and to highlight some of the distinctive issues that may be less important in other societies;
- to contribute to the existing stock of knowledge regarding accounting, management and control issues with specific illustrations from Libya.

Research questions are important to define the scope and focus of the research study (Eisenhardt and Bourgeois, 1988). In order to achieve these aims this research attempts to answer the following questions:

- What kinds of MCSs and accounting systems are currently applied in the Libyan case study enterprises, from the key industrial sectors, and why were they implemented in the way that they were?
- What are the contextual factors that influence and shape the MCSs and accounting systems in the privatised factories? What is the general interaction with the environment?
- How have the contextual factors influenced the MCSs in the Libyan private sector?
- Are there distinctive contextual factors that unusually complicate the management of privatised companies in Libya, in a way that reflect the uniqueness of the setting of their MCSs?

In order to further narrow the focus of the study, a few demarcations are necessary:



- The thesis focuses on specific organisations (Libyan case study enterprises, see section 1.2.2).
- The thesis deals primarily with the present, or recent, situation of the MCSs in the privatised factories<sup>1</sup>.
- The theoretical framework guides the researcher to look at specific themes and areas to gain an in-depth understanding of phenomena under investigation and to collect rich data from the research field (see section 1.2.2).

The selection of specific industrial cases so as to understand MCSs within their environment has some significant potential outcomes that can be summarised as follows:

- the describing of the actual characteristics and features of the MCSs of the organisations of the Libyan Food, Paper and Construction Materials industries;
- the findings of this research might encourage managers within the Libyan private sector to consider some radical revisions to their management control functionings and practise;
- providing the decision-makers with a clear view regarding actual MCSs in the industrial sector may help in the development of the planning and control processes;
- the understanding of the current MCSs in the cases industries of this research within their developmental environment is the first attempt to understand these relationships in Libya and consequently this study might be a departure point for many further studies.

This research, then, aims not just to theoretically examine the MCSs in the Libyan Food, Paper and Construction Materials industrial enterprises within their socio-political and economic context, but also to provide a basis for further research and to produce empirical findings that might be a useful guide in managing and controlling these enterprises.

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<sup>1</sup> Note that the factories became companies. They are not branches or parts of companies.



### **1.1.2 The reason for the choice of empirical sites: the significance of the industrial focuses**

The basic goal of industrial planning from 1970 to 1980 was to transform the Libyan community from a consumer community to a productive one and, to achieve this aim, many heavy industries were established<sup>2</sup>. During the period 1970-1993, the state invested 4,732 million LD<sup>3</sup> to develop and improve industrial activities, one of the development objectives being the establishment of another source of revenue in addition to oil. In the period between 1970 and 1994, the industrial sector as a whole has employed the largest proportion of the Libyan people (Gannows, 1999, p.323)<sup>4</sup>. The period 1986-1993 was significant as most of Libya's industrial objectives were restructured according to the perceived Libyan social, political and economic needs. An important target of the new plans was to shift from public ownership to private ownership and in doing this, many public factories were financially restructured and transferred to private ownership. Since 1987, The General People's Committee for Industry has issued a succession of executive decrees, to transfer the ownership of small/medium enterprises within particular sectors from the public to the private sector (The Ministry of Industry, 2000). These ostensible major changes to the industrial sector are a worthy focus of exploration (see Gannows, 1999; The General People's Committee, 2001).

For the purposes of this research, a group of Libyan factories was chosen to constitute case studies – one from each of the food, paper and construction materials sectors. These factories had been a part of the Libyan public sector (see Chapter 5). They are ostensibly becoming private sector companies. According to the general development plan of the country for the privatisation of certain factories from the public sectors, seventeen food, ten paper and ten construction materials factories were to become

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<sup>2</sup> For the definition and classification of heavy industries, see chapter 5.

<sup>3</sup> LD = Libyan Dinar (the official exchange rate is 1LD = £ 2 according to the Central Bank of Libya, 2002).

<sup>4</sup> The number of workers in the industrial sector in 1970 was 20,400. It increased to 81,969 workers by 1994. The industrial product was increased to 1,297 million DL in 1993 and the contribution of the industrial sector rose from 1.7% in 1970 to 7.4% in 1992.



private organisations (see Table 5.3). The reasons for the selection focused on here are as follows:

1. They are significant in the Libyan economy as they reflect the trend to become more independent or self-sufficient, especially through industries such as construction materials whose only dependence is on local raw materials.
2. The industrial sector, specifically the Food, Paper and Construction Materials industries, is regarded as a new area for research. Moreover, there are no existing empirical studies within the context of developing countries focusing on this substantive topic (MCSs of private sector industrial enterprises).
3. The influence of the Libyan public sector on private factories after the privatisation process has not been explored or considered by accounting researchers.
4. The researcher has been able to arrange reasonable access to the personnel and documents of the factories under research and can thereby obtain and gather sufficient data for an in-depth understanding of the phenomenon under investigation.
5. Despite now being recognised as extremely important, the change of ownership in the case study enterprises has been neglected by Libyan researchers for many decades. This change (privatisation) was as a result of the perceived failure of public organisations to achieve their development objectives, which encouraged the shift to the private sector<sup>5</sup>.
6. The importance of the Food, Paper and Construction Materials industries led to this researcher selecting them as case studies in order to develop an understanding of the ways in which MCSs operate in these Libyan businesses of significance and to provide an understanding of why these practices operate in the ways that they do.
7. Since the 1980s, the case study enterprises have been given more attention by Libyan decision-makers as playing an essential role in Libyan economic development (see Chapter 5). The exploration and understanding of the MCSs in

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<sup>5</sup> In another context, Storey and Johnson (1987), on the UK, stated that the increase in the importance of small and medium enterprises was the result of a weak performance of large companies in the manufacturing sector. Such insights have boosted research into the small and medium enterprise sector.



these Libyan industrial factories within their context will add to existing studies in different contexts.

#### **1.1.2.1 The reason for the choice of the particular organisations under study**

The Al Nur Factory (hereafter, ANF), the Libyan Fallah Factory (hereafter, LFF) and The Bricks Factory (hereafter, TBF) were selected for this research for a number of reasons. The factories are the only factories to produce the kinds of products they do in the mid-west of the country and thus have access to a large market. Also, both the ANF and the LFF operate in a competitive context with significant competition from imports, but, are confronting a situation encompassing state interference, shortages in raw materials and the payment of huge taxes. These burdens may, therefore, indicate to some extent how factories had fared under these conditions. Indicating the importance of the products of the factories, the ANF plays a significant role in the region because it meets around 90% of the local demand for paper notepads. Because of the quality of its product, the LFF is the only factory that produces recommended pear juice for hospitals, schools and nurseries. What is more, 90% of the raw materials for TBF were available locally. Hence, its ability to compete was very high. In contrast, the LFF and ANF had 90% dependency on state-controlled imported raw materials. The selection incorporates a broad range of types of organisational experience in this respect. A further key reason for selecting LFF, ANF and TBF was that the researcher was familiar with these factories. Ease of access to these factories and availability of assistance in collecting particular documents appropriate for the research were important factors for this selection. Not only the access to these factories but also the empirical work for this research required the researcher to be in the field for a long time (around six months). Thus, in order to achieve the stated objectives, specific enterprises in the Food, Paper and Construction Materials sectors have been chosen as case studies for this research. The case study is preferred, as the researcher wants an in-depth understanding of the organisational phenomena within their real-life context (Yin, 1994, see also Chapters 2 and 5).



### **1.1.3 The contribution of the study**

From the above, it is hoped that this study will contribute to the existing literature in a number of ways. First, the Libyan environment is different from Western world environments (socio-economically and politically), so this study might well provide a different description and analysis of the MCSs and an understanding of the relationships between organisations and their environments. Second, one of the research objectives was to explore and understand the impact of the Libyan privatisation experiment on accounting systems, so it is likely to provide new and different ideas about the influence of change in the context of the privatisation process of Libyan organisations upon the shaping of MCSs in these organisations. Third, this study will be conducted in a developmental environment, so its findings might help to improve and develop the existing MCSs in the Libyan context. Fourth, this study will contribute further to case study evidence that has emerged in other economies by providing evidence from a sample of Libyan private organisations. This evidence is compiled through an understanding of the current MCSs in the Libyan private sector. Finally, this research is the first attempt to understand the existing MCSs in the Libyan Food, Paper and Construction Materials industries in their context and also the first study that attempts to consider and understand the MCSs in the Libyan privatised factories and hence could be the basis for further studies.

## **1.2 Theory, methodology and method**

### **1.2.1 Systems ideas**

The MCSs can have many inter-related elements, which must be considered together, both systemically and holistically, in order to gain a better understanding of the complexity of the total control process within an organisation. According to Phillips (1977), systems are holistic, i.e. the whole is more than the sum of its parts and also determines the nature of its parts. What is more, the parts cannot be understood in isolation from the whole and the parts are dynamically inter-related and interdependent (cited in Otley, 1983, p.70). Lowe and Puxty (1989, p.17) described the importance of



general systems theory (hereafter, GST) as follows; “The most basic message of cybernetics and general systems theory is that control of an organisation is dependent on its being able to control its relationship with its environment.” Thus, in order to gain a better understanding of MCSs in the Libyan industrial sector, it was considered necessary to understand the MCSs within the context in which they operated (see, for a developed critical appreciation of this notion, Hopwood, 1983; Neimark & Tinker, 1986).

The word ‘system’ is used primarily to cover the systemic nature of the organisation that is being managed, its internal relationships and its interaction with its wider environment. Furthermore, the central meaning of a systems approach is that it seeks to explain behaviour by means of studying the interrelationships of the parts of the system rather than by merely studying the nature of the parts themselves (Otley, 1983). In this thesis, one aim is to attempt to understand the influence of the environmental factors upon the organisations under investigation. Using systems ideas in this study enables the researcher to gain a better understanding of the relationship between socio-political and economic factors and organisational processes such as MCSs. Systems concepts help in understanding the match between the internal structure of an organisation and the processes and characteristics of its environment.

The structure of an organisation can, arguably, be divided into three subsystems: a decision and control subsystem, a financial subsystem, and an operations subsystem (Lowe and Tinker, 1979) (see Figure 1.1). In order to understand the accounting practices in an organisation, the practices must be put into a whole organisational and social context. Otley (1983) suggested that the use of systems ideas in studying MCSs helps in understanding an organisation as a single system instead of considering its parts as isolated components. Thus, there is a conscious attempt to be holistic rather than reductionist in approach. Otley further argued that the systems ideas offered a method of studying management control and thereby had the potential to begin to deal with some of the underlying problems of management control. Accountability is an issue that has been raised in respect of MCSs (Roberts and Scapens, 1990, 1985).



Generally, systems of accountability in organisations can be seen to provide for the ‘binding’ of organisational time and space and to be a part of an organisation is to be subject to the system of accountability of that organisation. Accountability in its wider sense refers to the giving and demanding of reasons for conduct. Roberts and Scapens (1985, p.85) stated, for example, with regard to the customers/employees relationship, that the latter group is typically accountable, but the former is not. This demonstrates that accountability with respect to MCSs tends not to transcend the organisation boundary.

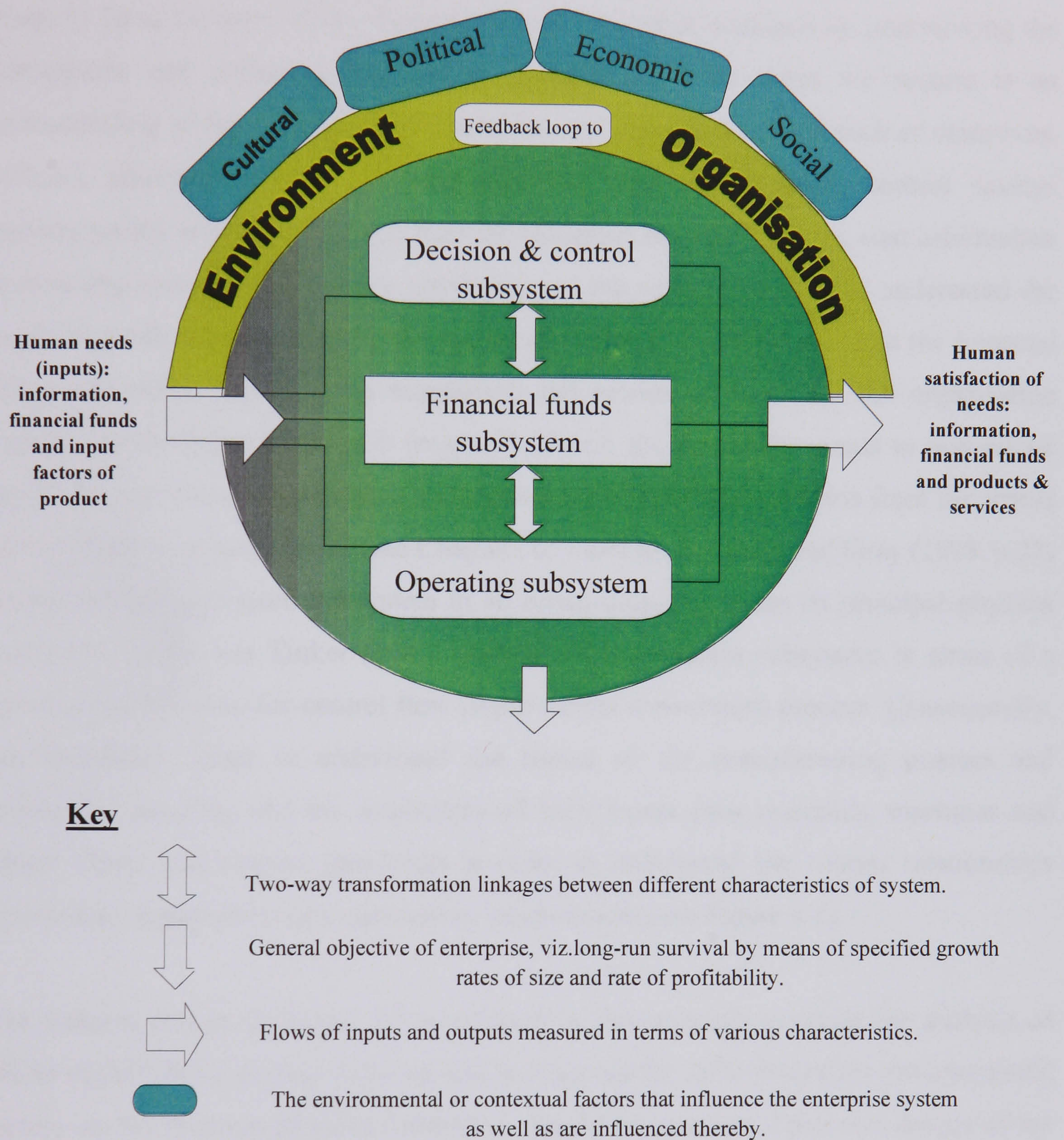
For the purposes of this research, systems theoretic ideas are used to focus on key elements of MCSs in order to explore and to understand these in terms of an interpretive research perspective. This thesis therefore attempts to understand the relationships between the factories under study and their environment and to explain the influence of the environmental factors on the functioning of MCSs. It is assumed that an organisation has a relationship with its environment so an open systems approach is adopted. An open system is a set of elements standing in interrelation amongst themselves and with the environment. Open systems engage in exchange transactions with their environments so they exchange information, products, labour and funds. An organisation that is not interacting and responding to its environment could not survive or grow over any period of time (Albanese, 1981). Lowe and Puxty (1989, p.24) stated that “[o]pen systems approaches to [studying] organisations are fruitful.”

It is argued that the environment of the organisation has a crucial role in the organisation’s success. Lowe and Puxty (1989, p.17), for instance, stated that “[t]he organisation exists because there is a need for it within the environment: and conversely, the organisation is dependent on its environment for resources.” MCSs regard an organisation as a controlled system, open to and interacting with a wider environment. The adoption of a ‘systems’ approach is to provide a description of the internal structure of an organisation, which consists of a set of defined elements (a set of parts) interacting together. In general, this set must cover the activities, operations, people and institutions of the organisation relevant to the understanding and explanation of the behaviour of any particular organisation as a social and financial entity. The

relationship between the system and its environment is of great importance as the system is dependent on the environment for its inputs and, conversely, the system (organisation) satisfies the environment's needs by returning its outputs. Lowe stated that "these inputs relate to the needs of people for the satisfaction of which the enterprise exists, and the outputs to the satisfaction of those needs" (Otley, 1989, p.33; Lowe and Tinker, 1981; Lowe, 1979, p.60).

For the purposes of this research, the internal structure of the system of an enterprise according to the work of Lowe and Tinker is adopted as a guide to provide for a descriptive and interpretive analysis of the case studies of this research. The internal organisation system is divided into three subsystems: the decision and control subsystem, the financial funds subsystem and the operating subsystem. These three subsystems are interrelated in that they are partial images of each other and all together complete the structure of the organisation (Lowe and Tinker, 1981, p.13; Lowe, 1972) (see Figure 1.1). In order to understand the subsystems of the organisations in this study, the researcher needs to gain key insights into every subsystem. The decision and control subsystem consists of "its brain (the top managers) and its executive 'arm' (those who execute the enterprise's formal policies, procedures and accounting control devices laid down by top management)" (Lowe and Tinker, 1981, p.17; Lowe, 1972).





**Figure 1.1: The internal subsystems of an industrial company in its environmental context.**

*Source: Derived and adapted from Lowe and Tinker (1981, p.18) and Lowe (1972)*



To gain a better understanding of the decision and control subsystem, the researcher needs to focus on some basic elements in order to gather evidence by interviewing the participants and collecting the relevant documents. Thus, what we require is an understanding of the organisational MCSs focused upon phenomena such as objectives, policies, structure (formal and informal), the accounting system, control devices (pricing policy and budgeting and how the managers use, for instance, cost information in planning and controlling their activities) and the reward system. To understand the financial funds subsystem, Laughlin and Gray (1988, p. 27) suggested that the financial funds subsystem “governs the acquisition and receipt of funds for the organisation (input) and the payment of cash (output)”. Hence, the researcher needs to understand sales and other revenues systems, and expenses and purchases systems from the words and experience of participants (see Chapters 6, 7 and 8). Laughlin and Gray (1988, p.27) stated that the operations subsystem in an organisation “governs its principal physical activities”. Lowe and Tinker (1981) described the operation subsystem in terms of a two-way information-for-control flow (input-output conversion) process. Consequently, the researcher needs to understand the basics of the manufacturing process and production planning and the acquisition of both inputs (raw materials, machines and labour force) and outputs (products) in order to understand the control relationships between an organisation (system) and its environment (see Figure 1.1).

The systems design in Figure 1.1 is adopted in this research to guide the analysis of MCSs in the Libyan private factories and to illustrate the influence of the environmental factors on the function of these systems. It should be mentioned that this design of the subsystems and elements of the system of an organisation is used as a guide or a basic check-list of those elements considered relevant to the design of MCSs in the organisations under investigation. This design does not hinder the exploration of other avenues, which may appear fruitful as each case progresses. It is worth clarifying at this point that the aim of using the framework in Figure 1.1 is to focus the researcher’s attention on what to cover in the empirical site but not to overly restrict the exploration (see Chapters 6, 7 and 8). Yin (2003, p.23) supported the idea of using a framework in this way: “Without such propositions, an investigator might be tempted to cover



‘everything’, which is impossible to do.” Yin continued by noting that relying on theoretical propositions (or what might be considered focuses about which skeletal propositions are made) is the most preferred strategy to guide the analysis of case studies, as the propositions help to focus attention on certain data and to ignore other data (Yin, 2003). Using a systems approach allows the researcher to gain a broader understanding of the phenomenon under investigation. The researcher found that using systems ideas for this research was best developed through an interpretive perspective (the interpretive approach will be discussed in more detail in Chapter 2).

Many accounting textbooks and much research on accounting systems are concerned with the fact that each country needs its own accounting systems according to its cultural and environmental conditions and should not simply borrow systems from other contexts (Hopwood, 1983; Briston, 1990; Wallace, 1990). Consequently, accounting systems and their implementation in differing countries differ according to their respective environments. For Libya, the contextual factors are different from those of the Western World, and indeed from other Third World countries (see Chapter 4). The Libyan economy was dependent on oil revenues for financing most of the country’s activities until the late 1980s when decision-makers in the government emphasised the importance of finding alternative revenue sources. The chosen area for the goal of improving and developing the Libyan economy was the industrial sector and many important steps to evaluate and reform the industrial sector took place in the period from 1987 until 1993. This is evidenced by, for example, the privatisation of some public companies (see Chapter 5).

### **1.2.2 Research methodology and methods**

In order to explore and understand the phenomenon under investigation (identified above), both methodology and data collection and analysis methods are considered. Methodology can be defined in many ways. For Taylor and Bogdan (1984, p.1), methodology is a way of thinking in order to achieve the objectives of the research. Further, methodology indicates the philosophy of method, incorporating philosophical assumptions brought to a research setting (Gioia & Pitre, 1990). For Strauss and Corbin (1998, p.3), methodology is a means to study and understand social reality. To achieve



the objectives of this thesis, multiple methods of data collection from the Libyan case studies context were selected (interviews, observation and document analysis).

For the purposes of this research, an approach with an interpretive emphasis (with the relevant qualitative methods that it prefers) was adopted<sup>6</sup>. This researcher adopted the case study approach to achieve the objectives of this study as this approach offered a chance to conduct intensive observations of enterprises and could be argued to be the best method to understand phenomena in their natural contextual setting. Scapens (1990), for example, notes the value of studying management accounting in everyday life through case studies and asserts that case studies offer the possibility of understanding the nature of MCSs and MASs in practice, both in terms of the techniques, procedures, and systems used, and the way in which they are used and their consequences.

The nature of the research is an important factor in shaping the method of data collection and analysis. In order to explore and understand the current situation of the MCSs in the Libyan Food, Paper and Construction industries, the researcher was not able to be far from nor to be uninvolved in, the social phenomenon he was interested in. Hence, the concern had to be to obtain and then maintain close contact between researcher and researched so as to discover, interpret and understand the views of participants about social reality. Although the case study approach has been criticised in that its findings cannot be generalised, the aim of this research was to provide a sound understanding of the current MCSs in the Libyan industrial context rather than to make generalisations. Yin (1994, p.13) defined the case study approach as “an empirical enquiry that investigates a contemporary phenomenon within its real-life context, especially when boundaries between phenomenon and context are not clearly evident.” For this research, the case study approach was, arguably, the most appropriate given the necessity of being in near proximity to people in the Libyan industries selected so as to understand their opinions and to explore issues related to MCSs. In addition, the case study approach combined with a number of data collection and analysis methods is

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<sup>6</sup> The interpretive approach will be elaborated upon in the next chapter.



known as ‘triangulation’. Ideally, one source of evidence will corroborate another to some extent (Stake, 1995).

### **1.3 The structure and organisation of the thesis**

The thesis consists of ten chapters (see Figure 1.2):

Chapter 1 is the introduction, which provides a background to the research area, explains the objectives, research interest, theoretical framework, a brief discussion of research methodology and method and the contribution of the study.

Chapter 2 looks at the methodology that is employed in this research and the data collection and analysis methods.

Chapter 3 presents a literature review of management control in Third World countries including Libya.

Chapter 4 provides an overview of the social, economic, and political environment of the Libyan Food, Paper and Construction Materials industries (industries in which the case studies are located). It provides a description of the Libyan environment at a macro level within which the organisations under investigation operate.

Chapter 5 provides an overview of the Libyan industrial sector and highlights industrial development plans and the official procedures for ostensibly transferring the ownership of public factories to private ownership.

Chapter 6 details the first case study, provides an elaboration of the organisational context of The Libyan Fallah Factory and identifies the major issues related to MCSs in this company.

Chapter 7 details the second case study, provides an elaboration of the organisational context of the Al Nur Factory and identifies the major issues related to MCSs in the industrial sector.

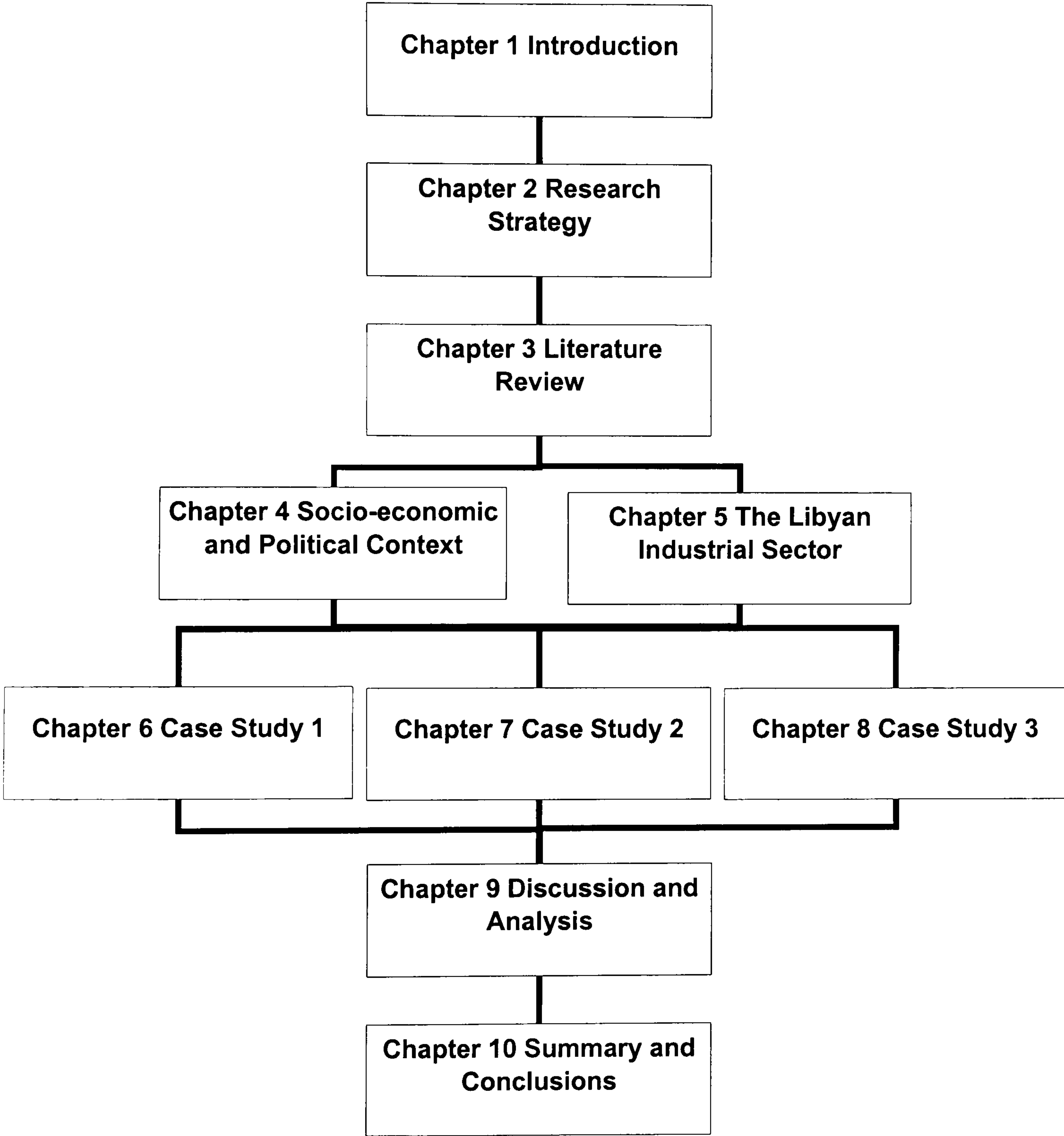
Chapter 8 details the third case study and presents a descriptive analysis of the organisational context of 'The Bricks Factory' and identifies the major issues related to MCSs in the industrial sector.

Chapter 9 provides a discussion and analysis of the existent MCSs in the research cases.

Chapter 10 contains the conclusions, recommendations and suggested avenues for further research.



**Figure 1.2: The structure of the Thesis**



## **Chapter 2: Elaboration of the Research Strategy**

### **2.0 Introduction**

The broad topic of interest of this research is to understand the MCSs within their developmental context in the Libyan private industrial sector. More specifically, the target of this research is to explore and gain in-depth understanding of the current situation of the MCSs in the Libyan Food, Paper and Construction Materials industries within their environmental organisational context. The objective of this particular chapter is to describe the research strategy to accomplish these research aims. This chapter is hereafter divided into sections as follows: research methodology, research methods, and a conclusion and summary of the chapter.

### **2.1 Research methodology**

This study aims to “pay close attention to the socio-economic and political contexts in which organisations operate and are developed” (Broadbent, 1992, p.343). Having chosen a research topic, appropriate methodology must be located, explored, described, explained and interpreted (Marshall and Rossman, 1989). The way in which the researcher aims to achieve the objectives of this research is to understand the relationship between socio-economic and political factors and organisational processes such as MCSs in the Libyan case study industries. Taylor and Bogdan (1984, p.1) stated that methodology “refers to the way in which we approach problems and seek answers ... [it] applies to how one conducts social research”. Methodology also means the underlying philosophy of method and assumptions that a researcher brings into a research setting (Gioia & Pitre, 1990). Strauss and Corbin (1998, p.3) defined methodology as “a way of thinking about and studying social reality”. Berry (1983) argued that the process of developing knowledge depends upon the methodologies used and that methodology is not just about data collection and the rules for evidence; in its



large conception it is about the nature of explanation and the means by which explanations are produced.

It should be remembered that research methodologies do not stand in isolation of researchers' beliefs; on the contrary, they are closely related to each other. The ontological and epistemological assumptions of researchers influence and shape their methodology, because each one has implications of a methodological nature and, different social theorists are drawn towards different methodologies (Hopper & Powell, 1985). Ontological assumptions relate to the form and the nature of reality [and come before the epistemological assumptions] because Ontology is "the study of being" (Crotty, 1998, p.10). Different ontological assumptions are associated with different epistemological assumptions and influence methodologies as epistemology refers to "the theory of knowledge embedded in the theoretical perspective and thereby in the methodology" (Crotty, 1998, p.3). Thus, researchers' ontological beliefs about the organisational phenomenon affect both their epistemological assumptions and their methodological assumptions (Chua, 1986). Epistemology, encompassing beliefs about the nature of knowledge for any phenomenon under investigation (Gioia & Pitre, 1990) can be described as "what is to count as acceptable truth by specifying the criteria and the process of assessing truth claims" (Chua, 1986, p.604). Epistemology also addresses the question "what is the nature of the relationship between the knower or would-be knower and what can be known?" (Guba and Lincoln, 1994, p.108), as that which can be considered as true knowledge is defined as part of epistemology. Epistemology precedes research methodology (see Burrell and Morgan, 1979; Gill and Johnson, 1997).

The nature of dealing with the external environment can be identified differently in different societies, and even in different organisations within the same context. Moreover, the response of MCS processes can differ according to different contexts. The Libyan environment is different from a Western environment; a point that is borne out and exemplified by this research, as this study is the first to deal with MCSs from companies in the Libyan private Food, Paper and Construction Materials industries. This different approach requires a conceptual understanding of the MCSs process in



their organisational and environmental contexts and their wider socio-economic and political environment so as to understand better the actual MCSs in these organisations (see Chapter 4).

- **Burrell and Morgan's paradigms**

Burrell and Morgan (1979) reflect the above discussion by describing a theoretical framework based on the idea that “all theories of organisation are based upon a philosophy of science and a theory of society” (Burrell and Morgan, 1979, p.1). The framework has been understood to be applicable to studies of social phenomena in general. Thus, a researcher's beliefs about the nature of the social world and society provide a basis for the selection of suitable theoretical assumptions. Burrell and Morgan (1979) divided the different theories related to social science and society into two dimensions [within one framework]; the Subjective-Objective dimension on the one hand and the Regulation-Radical dimension on the other. Researchers adopting the theory of regulation view the society as basically not in need of change, but researchers at the other end of this scale adopted the theory of radical change because they believed that conflict in a society indicates society in need of change.

In the first dimension, the two contrasting dimensions are identified as Objectivist and Subjectivist approaches. The subjectivist approach postulates that the social world is made up of nothing more than names, which are created by people to perceive reality and communicate with each other. In its extreme form, the subjectivist does not admit to there being any “real” in the social world. The Objectivist, however, assumes that the social world is external to the individual and consists instead of real, hard, tangible elements with a constant structure, and that social reality is not something the individual creates (Burrell and Morgan, 1979; Blackwell, 1985; Kolakowski, 1993). In terms of this thesis, conducting research into the Libyan developmental environment, the researcher needs to be close to people to understand their real world from their words and expressions in order to understand the relationship between the environmental factors, which are created by people and organisational processes such as MCSs in the



present case studies industries. Therefore, the subjectivist approach was more appropriate for this research.

According to the two ontological approaches, the differences between qualitative and quantitative research are identified; [objectivism tends to place an emphasis on the quantitative but subjectivism tends to place an emphasis on the qualitative]. Therefore, reality in quantitative research is objective, real, autonomous, and can be measured by using some selected methods (Creswell, 1994). Quantitative methods rely mainly on hypothesis testing using scientific methods of analysis. Qualitative approaches, on the other hand, attempt to understand the social world only by first-hand knowledge of the phenomenon under investigation through methods such as observations, interviews, and document analysis (see Table 2.1).

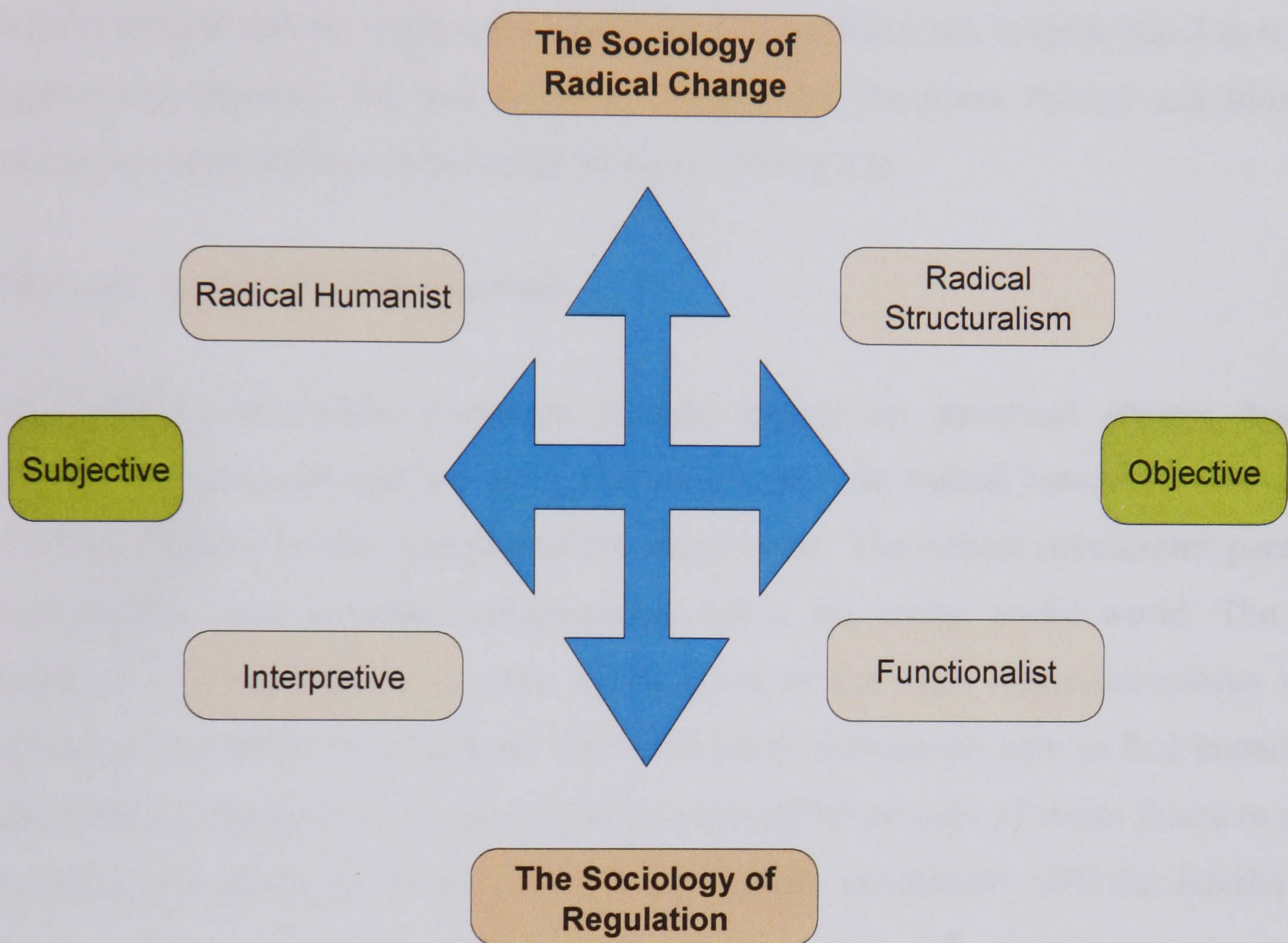
Table 2.1 Assumptions of the Objectivist and Subjectivist Dimensions.

Assumption	Question	Objectivist	Subjectivist
Ontological	What is the nature of reality?	Reality is objective and singular, apart from the researcher	Reality is subjective and multiple as seen by participants in a study
Epistemological	What is the relationship of the researcher to that researched?	Researcher is independent from that being researched	Researcher interacts with that being researched
Methodological	What is the process of research?	Deductive process Cause and effect	Inductive process mutual simultaneous shaping of factors
		Static design-categories isolated before study	Emerging design-categories during research process
		Context-free  Generalisation leading to prediction and understanding  Accurate and reliable through validity and reliability	Context-bound  Patterns, theories developed for understanding  Accurate and reliable through verification

Source: Adapted from Creswell (1994, p.5).



**Figure 2.1 Burrell and Morgan (1979, p.22)**



Burrell and Morgan (1979) also identified another two major dimensions of society. One is related to regulation, order, stability, and tries to explain why a society tends to hold together. The second one focuses on the fundamental division of interest, conflicts, and unequal distribution of power that would lead to radical change in society. These dimensions are known as the “order-conflict” debate. The “order-conflict” debate reflects the researcher’s opinion of the nature of the phenomenon under investigation. If the researcher believes that there is a need to make changes in society, this would



suggest the adoption of a conflict-radical society approach. In contrast, if the researcher's aim is to maintain the current situations, the adoption of an order-regulation approach is necessary (Burrell and Morgan, 1979). These two independent dimensions (social world and nature of society) are combined in one framework and this framework creates four interactive but mutually exclusive paradigms. These four paradigms are: the functionalist, the interpretive, the radical humanist, and the radical structuralist. It is helpful to note that the interpretive approach will be discussed in more detail as it is the appropriate approach for this research. Figure 2.1 illustrates Burrell and Morgan's paradigm (adapted from Burrell and Morgan, 1979, p.22).

### **The radical structuralist approach**

The radical structuralist paradigm focuses mainly on structural change from an objectivist standpoint and has many similarities with the radical humanist paradigm, as it adopts the idea of the changing of the social order. The radical structuralist paradigm concentrates upon structural relationships within the realist social world. The main target of this paradigm is to seek explanations of the basic interrelationships in the context of the total social pattern. There are many debates on how to find knowledge, and different theories within this paradigm posit different roles of social forces to give a meaning or explanation of social change (see Hopper and Powell, 1985 for details).

### **The functionalist approach**

A functionalist paradigm represents the objectivist perspective of the social world, and is rooted in the sociology of regulation. It attempts to explain from an objectivist viewpoint the regulation, integration, consensus and solidity of societies between their fundamental components from an objectivist viewpoint. The approach uses causal relationships that emerge from reality in an effort to explain social phenomena in society but without any intention of changing it. Hence the goal is to understand the relationship between regularities with the subject being studied. This approach seeks to provide essentially rational explanations of social problems, and it is a way of generating knowledge, which can be put to use for future studies. This paradigm postulates that the social world is concrete, hard, real, and controlled by the



environment and accordingly, this paradigm uses quantitative methods to explain the phenomenon under investigation (see Chua, 1986; Hopper and Powell, 1985).

### **The radical humanist approach**

The radical humanist paradigm focuses on radical change in societies from a subjective standpoint. This approach shares the characteristics of the interpretive approach with respect to the subjective nature of the social world where reality tends to be nominalist, anti-positivist, voluntarist, and ideographic. The basic illustration of this paradigm is that participants interact with the dominant ideologies in society. This radical humanist paradigm also pays a lot of attention to the mode of domination, the main aim being to free the members of a society from the sources of domination, thus trying to change the social world through changing the pattern of human behaviour (Burrell and Morgan, 1979; Gioia & Pitre, 1990).

### **The Interpretive approach**

The interpretive paradigm is informed by a concern to understand the social world as it is, without any intention of making any changes in it. It tries to explain the regulation and order of society from the level of subjective experience. The main focus of the interpretive paradigm is to understand the phenomenon under investigation. Burrell and Morgan (1979) defined the interpretive approach thus:

“Its subjectivist approach to the analysis of the social world makes its links with this sociology often implicit rather than explicit. The interpretive paradigm is informed by a concern to understand the world as it is, to understand the fundamental nature of the social world at the level of subjective experience. It seeks explanation within the realm of individual consciousness and subjectivity” (Burrell and Morgan, 1979, p.28).

Gill and Johnson (1991, p.126) suggested that the interpretive approach tries to “understand how people make sense of their worlds, with human action being conceived as purposive and meaningful.” The interpretive approach believes that knowledge acquired and transmitted should be understood from the point of view of the actors



involved in daily activities. Thus, involvement in the field, and being a participant will improve the researcher's understanding of the social world. Hopper *et al.* (1987, p.438) argued that the interpretive approach is a "label employed to signal a commitment to appreciate social phenomena from the standpoint of the actors who are engaged in the routine construction and reproduction of social worlds". There is a growing call for more interpretive approaches and subjective studies to improve the understanding of accounting and control systems in their organisational context (Hopper *et al.* 1987; Nahapiet 1988; Chua 1986). Interpretive approaches provide a focus on organisational processes (such as MCSs), in particular on how the reality of organisations is produced and reproduced by actors (Colville, 1981). Chua (1986, p.618) argued that the interpretive approach offers an understanding of accounting in practice, seeks the actor's opinion and definition of the situation and analyses how this is woven into a wider social framework. Qualitative methods are more appropriate than quantitative methods in studying the social construction of subjective human reality. Strauss and Corbin (1998, p.11) stated that "[q]ualitative methods can be used to explore substantive areas about which little is known or about which much is known to gain novel understandings. In addition, qualitative methods can be used to obtain the intricate details about phenomena such as feelings, thought processes, and emotions that are difficult to extract or learn about through more conventional research methods". For Hopper and Powell (1985, p.447) "[t]he suggestion is that by using interpretive research methods to study how accounting meanings are socially generated and sustained, a better understanding of accounting will be obtained."

The interpretive approach tends to be nominalist, anti-positivist, and voluntarist. It perceives the social world as one of individual creation, and the idea of the real existence of the social world is completely rejected. Interpretive philosophers and sociologists seek to understand the basics of social reality by becoming involved in daily activities. This involvement contributes to improving the researcher's ability to understand the reality of the social world. According to this paradigm human nature is independent, and all environmental circumstances can be modified. The appropriate research methods for this approach are qualitative because they can be applied at the site of the phenomenon being investigated. All the research methods aim to obtain close



contact with the research context such as interviews, observation, document analysis (Chua, 1986; Strauss and Corbin, 1994). Thus, the interpretive perspective to management control could be, arguably, the most appropriate approach to provide a better understanding of the social, political and economic influence on the MCSs in the Libyan organisations under investigation.

Tomkins and Groves (1983) suggest that researchers who want to avoid the historical descriptive studies of organisations, almost universally select a scientific research style, which involves many stages to achieve their studies. Starting with a theory formulated in terms of relationships between categories more often than not based on ideas emanating from previous academic literature, then the theory is used to establish the research problem, which is transformed into hypotheses and into independent and dependent variables. An accurate and precise process is followed for data collection (always in numerical form). This collected data is then processed by mathematical or statistical techniques leading to an almost exclusively quantitative validation of the hypotheses tested. It is worthy of note that most of the social areas are dominated by scientific research approaches, but there are still some areas that have never been covered and these areas have become increasingly exhorted by advocates to use more naturalistic approaches by greater use of qualitative data (Tomkins and Groves, 1983).

Blumer (1978) challenged the conventional “scientific” approach as a way of understanding the social world by arguing that:

“This conventional protocol of scientific analysis is not suitable or satisfactory for the kind of analysis that is needed in direct examination of the empirical social world ... [it] forces ... data into an artificial framework that seriously limits and impairs general empirical analysis. Scientific analysis requires two things: clear discriminating analytical elements and the isolation of relations between these elements. The conventional protocol does not pin down in an exact way the nature of the analytical elements in the empirical social world nor does it ferret out in an exacting manner the relation between these analytical elements” (Blumer, 1978, p.41).

Researchers interested in studying and investigating behaviour relating to accounting and, gaining the ‘value’ of different accounting procedures, need to move away from



using mathematical analysis and modelling, statistical tests, surveys and laboratory tests because these research techniques are not associated with specific real world problems in the sense that they do not relate to specific decision contexts. This thesis aims to explore and understand the actual situation of MCSs implemented in the Libyan private organisations within their developmental environment. Tomkins and Groves (1983) supported research based field-work by arguing that:

“[S]uch academics might profitably move more into detailed field-work (i.e. recording what is happening in the setting within which decisions are made and action occurs) and focus rather more on studying how practitioners perceive their worlds, what issues concern them, why these issues concern them and how they perceive them affecting accounting practices and the influence accounting has. In this way it is far more likely that academic research can be linked up with practitioners and their views of the world; in this way it is more likely that reliable theories about the effects of alternative accounting procedures can be developed” (Tomkins and Groves, 1983, p.364).

Blumer (1978) argued that to study and understand the research problems, which concern social behaviour, the ‘scientific’ model is not just difficult to manage, but is also manifestly inappropriate. Hence, a ‘scientific’ model of research is only suitable when the understanding of reality needs to use independent and dependent variables and statistical testing of the relationships between them. Therefore, it is inappropriate for this study because it attempts to understand the social world only by first-hand knowledge and to be close to people to understand their real world from their words and experience.

### **2.1.1 Factors affecting the choice of methodology**

The choice of methodology for this study is based on several factors, related to both the researcher’s beliefs and also the nature of the research topic as the central objectives for research can guide the research strategy. Many researchers (Glaser and Strauss, 1967; Marshall and Rossman, 1989; Creswell, 1994; Strauss and Corbin, 1998) suggested a number of factors to be influential in the selection of methodology by researchers. These factors may include the applicability of a given strategy, which should be determined by the extent of the control a researcher has over behavioural events (Yin,



1987). In addition, Creswell (1994) suggested that the audience before whom the study is performed influences methodology selection. In addition, the nature and purposes of the research problem, the degree of maturity of the relevant body of knowledge and budget and time constraints are factors that need to be taken into consideration by researchers (Pettigrew, 1990).

The research objectives are an important factor, which can guide the research process, and these objectives are originally derived from the researcher's goals. Some researchers may have the intention of challenging, changing and converting the dominant social norms while others might seek to create an understanding of what is happening merely to explore and investigate the situation. The former is likely to work in the radical paradigm because the investigation is intentionally geared to achieve change in the phenomenon being investigated. However, the latter is likely to be located in the regulation-order paradigm (Laughlin, 1995; Chua, 1986). Therefore, the individual characteristics that the researcher has can have serious implications for the whole research process. This researcher believes that conducting research in the Libyan private sector focusing on Food, Paper and Construction Materials industries to provide better understanding of the MCSs in their developmental environment is affected primarily by two factors: first, the researcher's beliefs in the subjective social reality, and second, the nature of the study and its consequent likelihood to fall within the interpretive approach to an in-depth understanding of the phenomenon under investigation.

The circumstances of the research, the interests and training of the researcher and the material required to build a theory dictate the dominance in a specific research situation (Glaser and Strauss, 1967). Furthermore, one of the fundamental and key decisions that researchers need to take in framing a research strategy is whether to follow a qualitative or quantitative mode of investigation, or a combination of the two. This helps researchers to clarify the direction of their study. The following section discusses the choice of paradigm and methodology for this particular research project.



### **2.1.2 Choice of methodology**

The nature of the study and the researcher's knowledge played an essential role in choosing the paradigm of study. As noted in previous section, the researcher believes that social reality tends to be more subjective than objective, that reality is created by the individual, and based on experience. According to Burrell and Morgan's (1979) paradigm this research topic can be located only in the radical humanist paradigm or in the interpretive paradigm. In order to choose one of these two paradigms, the objectives of this researcher and the nature of the research need to be clearly identified. The objective of this researcher is to explore and understand the relationship between socio-political factors, economic factors and organisational processes such as MCSs in Food, Paper and Construction Materials industries in Libya. It appears that this research seeks to "pay close attention to the socio-economic and political context in which organisations operate and are developed" (Broadbent, 1992, p.343). The phenomenon being studied in this research focuses on understanding the ways in which MCSs operate in Libyan industrial companies (the case studies) and to provide a better understanding of why these companies operate the MCSs in the way that they do.

The nature of the research problem should also be matched to the paradigm selected. Strauss and Corbin (1998, p.11) asserted that the nature of the research problem is essential when choosing a specific paradigm; "Qualitative methods can be used to explore substantive areas about which little is known or about which much is known to gain novel understandings. In addition, qualitative methods can be used to obtain the intricate details about phenomena such as feelings, thought processes, and emotions that are difficult to extract or learn about through more conventional research methods." The justification for qualitative research in social science becomes stronger when moving from an objectivist perspective toward a subjectivist perspective on the continuum of Burrell and Morgan's framework (Burrell and Morgan, 1979). Bryman (1992, p.61) suggested that "the most fundamental characteristic of qualitative research is its express commitment to viewing events, actions, norms, values etc. from the perspective of the people who are being studied." Qualitative methodology focuses on the importance of



understanding human behaviour and the organisational context of social interaction. Furthermore, according to the interpretive approach, social practices, such as accounting practices, are socially constructed. Ryan, *et al.* (1992, p.63) described the effect of social actors on the social practices as follows: “The starting point for such an approach is the belief that the social practice, such as management accounting practices, are not natural phenomena; they are socially constructed. Consequently they can be changed by social actors. This means that we should not be looking for universal laws and generalisations (as in the natural science), but for the rules, both explicit and implicit, which structure social behaviour. These rules, however, are themselves the outcome of social behaviour. In other words, social structures are both a condition and a consequence of social action.” Hence, this researcher needs to have a close involvement with the Libyan organisations under investigation in order to gain a better understanding of the role of MCSs in these organisations within their environmental developmental context.

This thesis requires a methodology that helps the researcher focus on and investigate the actual situation of the MCSs in the Libyan enterprises studied; therefore, the interpretive approach and qualitative methodology are, arguably, most appropriate for this research. No previous study has been conducted on the Libyan private sector concerning this subject, hence the subject needs an in-depth study so as to gain a sufficient and effective understanding of this area of study. All the recent requirements of the study are in the interpretive paradigm. Hopper and Powell (1985, p.466) argued that “understanding the conduct of others is obtained through a process of interpretation, or ‘typification’, rather than by direct observation – such ‘typification’ being continuously learnt, modified or reaffirmed throughout people’s lives ... people constantly create their social reality in interaction with others. It is the aim of an interpretive approach to analyse such social realities and the ways in which they are socially constructed and negotiated.”

The interpretive approach, with its qualitative methodology, has the ability to establish when and why perceptions change, and why some of them remain unchanged (Hopper and Powell, 1985). There are many reasons that encouraged this researcher to choose the interpretive approach for this study: first, MCSs in Libyan Food, Paper and



Construction Materials industries are new and have not been researched to date, thus the existing knowledge was not sufficient to make any *a priori* assumptions. Second, the existing literature related to the phenomenon under investigation was related to different environments and cultures, namely those from developed countries, i.e. countries different from the Libyan context where this study was to be conducted. Furthermore, hypotheses and assumptions derived from Western research may be different from the phenomenon being studied in the Libyan context. This interpretive approach is an attempt to “produce a rich and deep understanding of how managers and employees think, understand, interact with, and use” MCSs in their daily interaction (Macintosh, 1994, p.4). Hopper and Powell (1985, p.447) stated “[t]he suggestion is that by using interpretive research methods to study how accounting meanings are socially generated and sustained, a better understanding of accounting will be obtained.”

The main focus of this research will be on an understanding of the existent MCSs within their developmental context. One of the research interests is to compare the development objectives of the state at a macro level and the objectives of the case studies (factories) at a micro level in an attempt to establish whether there is any conflict between these two levels that could affect the function of MCSs. Furthermore, cost and pricing system, organisational objectives, structures and management, the budgeting system, reward system, and accounting system will be considered as a guidance in order to gain a better understanding of the existing MCSs in the Libyan private companies under study (see Chapters 6, 7 and 8).

## **2.2 Research method**

In terms of a definition, research can be defined as either qualitative or quantitative or as a combination of the two, according to the nature of the study. This study is focused on the Libyan industrial sector and the qualitative approach is required to gain an in-depth understanding of the nature of MCSs within their specific developmental environment. The qualitative paradigm enables researchers to get close to subjects by observing people's behaviour and actions in normal everyday life (Schutz, 1967).



This study has an inductive emphasis, the selection of which is made according to the nature of the study and the researcher's beliefs. Moreover, the attribute of this study is an explanatory one, which reveals the need for in-depth investigation to provide a sufficient perception and understanding of the phenomenon under investigation (Creswell, 1994). The existing literature related to the phenomenon under investigation focuses mainly on the context of enterprises in developed countries, and these countries have environments different from those of developing countries (in which Libya is included). Strauss and Corbin (1998, p.287) addressed this problem and suggested that overseas students who want to choose their countries as a research field to collect data should use qualitative methods as follows: "If a foreign student is studying here but wishes to collect data in his or her own country, then most certainly he or she can use this method or other qualitative methods. It is important that other countries do not borrow theories but instead, develop their own ones that reflect their societies' or citizens' cultures and behaviours." Qualitative methods can be used to uncover the nature of people's actions and experiences and perspectives, which are as yet little known in the world of research products. The qualitative approach consists of a number of different parts. In terms of qualitative analysis, this means any kind of analysis that produces findings or concepts and hypotheses, (as in grounded theory), that are not arrived at by statistical methods. Qualitative analysis may be done with data arrived at quantitatively or qualitatively or in some combination of the two approaches. Qualitative research is used when an understanding of a circumstance in terms of how and why it occurs is required (Cassel and Symon, 1994, p.5).

Positivist approaches to research insist on the precise objectives of the research in advance of the collection and analysis of data, yet what is known about this research topic is not sufficient to justify the specification of these objectives in advance. Hence, it is worthwhile for the researcher to enter the field to become familiar with the substantive area where the research will be conducted in order to identify matters and issues leading to an understanding of the actual situation of MCSs in Food, Paper and Construction Materials industrial enterprises.



In terms of the interpretive approach, Gill and Johnson (1991, p.126) suggested that the interpretive approach attempts to “understand how people make sense of their worlds, with human action being conceived as purposive and meaningful rather than externally determined by social structures, the environment or economic stimuli”. Strauss and Corbin (1998) emphasise that the researcher must enhance his/her “theoretical sensitivity” about the phenomenon under investigation to enable him/her to identify a specific research problem before going to the research site. This theoretical sensitivity allows the researcher to give meaning to the data, and enables him/her to identify the important issues to study. Researchers who have a background of the phenomenon under investigation are able to explore, explain, and clarify it. For this research, the theoretical framework provides basic propositions that help the researcher to focus on and collect relevant data (see section 1.2.1).

### **2.2.1 Case study approach**

Otley and Berry (1994, p.47) wrote that “case studies are likely to be most valuable where they are clear about their initial theoretical position and where they consciously attempt to develop their own theoretical modifications, however tentative”. Case study analysis, as “a methodology that examines a contemporary phenomenon in its real-life context” (Chua, 1982, p.178), has an essential role in researching the actual function of management accounting practices in organisations. Langfield-smith (1997, p.228) concluded that in studying MCSs the interactions are complex and probably only in-depth (case-based) research can help one understand the complex nature of these relationships. Ryan *et al.* (1992, p.113) argued that in the literature the terms ‘case study’ and ‘fieldwork’ are both used to refer to studies of accounting in its practical setting. Using a case study approach in this research is thus an appropriate way of gaining a better understanding of the MCSs in the Libyan private factories within their developmental environment. Ryan *et al.* (1992, p.113) further stated that “[c]ase studies offer us the possibility of understanding the nature of accounting in practice; both in terms of the techniques, procedures, systems, etc. which are used and the way in which they are used.” Case study analysis constitutes an approach that examines a contemporary phenomenon in its real-life context (Chua, 1982, p.178). It can have a



critical role in researching the actual function of the MCSs in the Libyan industrial organisations.

Case studies enable the researcher to collect data about MCSs from participants in their environment and also provide the flexibility to explore and understand issues related to the phenomenon being studied from their words and expressions. This researcher seeks to be in close proximity to personnel in Food, Paper and Construction Materials industries in order to gain an in-depth understanding of the current situation of MCSs within their developmental context. Drury and Tayles (1995, p.278) noted that “[t]here is now a need for case study research that explores in much greater depth how accounting information is used”. For the purposes of this research, three case studies from the Libyan case studies sectors were selected to gain a better understanding of the role of the MCSs in the Libyan private organisations within their environmental developmental context (see Chapter 5). In terms of the number of case studies that should be taken, Yin (2003, p.53) argued that “multiple-case designs may be preferred over single-case designs ... the chances of doing a good case study [with multiple cases] will be better than [those] – using a single-case design ... More important, the analytic benefits from having two (or more) cases may be substantial”. Therefore, three case studies were chosen for this thesis.

Case studies enable the researcher to collect data about MCSs from participants in their environment and according to their experience. Calls have been made for a greater commitment to more in-depth (case-based) research (Hopwood, 1983; Kaplan, 1986). Case study analysis enables the researcher to deal with a variety of issues. Ryan, *et al.* (1992, pp.114-115) suggested five types of case studies:

- The descriptive case study, which describes the current different accounting practices in the selection cases. The objective of this kind of case study is to provide a clear description of the accounting practices and highlight any gaps between theory and practice.
- The illustrative case study: this kind of case study aims to illustrate new innovations when they are being developed by companies.



- The exploratory case study: this type of case study is used when the nature of the study is to explore the reasons for the current accounting practices. These case studies allow for the generation of ideas, assumptions, and hypotheses. These hypotheses can be later tested on large samples.
- The experimental case study: this case study is used when the research attempts to evaluate the benefits and difficulties of implementing a new procedure or technique in practice.
- The explanatory case study: this type of case study aims to explain the reasons for observed accounting practices. The objective is to understand the practices rather than to produce generalisations (see sections below).

Spicer (1992) classified the above case studies into 1) Descriptive/explanatory and 2) Illustrative/explanatory. Group 1, i.e. descriptive and/or explanatory, case studies seek to describe/explore and explain reasons for particular accounting practice(s), whereas, group 2, i.e. illustrating and/or explanatory, are case studies used indirectly to help inform non-case empirical research, or used directly to explain observed practice. The primary objective of this study was to understand and explain the current situation of the MCSs in the Libyan private sector. Accordingly, the group 1 case study was considered most useful for this research.

It is argued by many that qualitative methods such as a case study approach in accounting research can make substantial contributions to the study of accounting systems in organisations (e.g. Hopwood, 1983; Otley, 1984; Scapens, 1990; Hopper & Powell, 1985). However, as with almost any research strategy, case studies are criticised by some researchers on a number of points:

- Case studies provide very little basis for scientific generalisation.
- There is a lack of rigour in case study research.
- Case study research takes too long and results in unwieldy, unreadable documents.



Yin (1994, p.33) suggested a number of strategies to avoid these criticisms, and these are set out in Table 2.2

Table 2.2: Case study tactics for four design tests.

Tests	Case study tactic	Phase of research in which tactic occurs
Construct validity	Use multiple sources of evidence	Data collection
	Establish chain of evidence	Data collection
	Have key informants review draft case study report	Composition
Internal validity	Do pattern-matching	Data analysis
	Do explanation-building	Data analysis
	Do time-series analysis	Data analysis
External validity	Use replication logic in multiple-case studies	Research design
Reliability	Use case study protocol	Data collection
	Developed case study data base	Data collection

Source: Adapted from Yin (1994, p.33).

Yin (1994) defined the four design tests as common tests to all social science methods and categorised them as follows:

- construct validity: establishing correct operational measures for the concepts being studied;
- internal validity (for explanatory or causal studies only, and not for descriptive or exploratory studies): establishing a causal relationship, whereby certain conditions are shown to lead to other conditions, as distinguished from spurious relationships;
- external validity: establishing the domain to which a study’s findings can be generalised;
- reliability: demonstrating that the operations of study, such as the data collection procedures, can be repeated, with the same results (Kidder and Judd, 1986).



The nature of the research is an important component to identify and influence the method of collecting data. As the main objective of this research is to explore and understand the current situation of MCSs in the Libyan Food, Paper and Construction Materials industries under investigation within their developmental environment, the researcher cannot reside far away from and be uninvolved in the social phenomenon which is under investigation. Hence, the role should be defined as obtaining and maintaining close contact between the researcher and researched in order to discover, interpret and understand participants' views about social reality. The case study approach is therefore an appropriate approach to adopt in this research. Although it has been criticised in that its findings cannot be generalised, the aim of this research is to provide a solid understanding of the current MCSs in the Libyan industrial context rather than to make generalisations.

Yin (1994, p.13) defined the case study approach as “an empirical enquiry that investigates a contemporary phenomenon within its real-life context, especially when boundaries between phenomenon and context are not clearly evident”. Another point about this research is that it aims to understand the actual situation of the MCSs in Libyan case study industries within their environmental developmental context, where little information is currently available. It aims to study and understand the phenomenon under investigation through people (the People's Committee and the Congress Committee members, accountants and those in charge in public parties such as the Ministry of Industry) in their own environment using multiple methods of data collection (interviews, observation and document analysis). Within social science, this approach is usually referred to as ‘triangulation’. Denzin (1970, p.3) supported the idea of using multiple research methods and wrote that “no single method is free from flaws – no single method will adequately handle all the problems ... and no single method will yield all the data necessary”. Interviews can give a chance for people to express their perceptions in their own words, to discover their problems. This helps the researcher to understand the influence of the environment factors on the MCSs in the Libyan private industries. For this research, a case study approach is appropriate to be in



close proximity to people in Food, Paper and Construction Materials industries in order to understand their opinions and explore issues related to MCSs.

- **Generalisation or particularisation**

Generalisation from a case study is not the main objective for researchers adopting this approach. Yin (1989, p.21) distinguished between theoretical generalisation and statistical generalisation; “[a] case study ... does not represent a ‘sample’, and the investigator’s goal is to expand and generalise theories (analytic generalisation) and not to enumerate frequencies (statistical generalisation)”. The case study approach, which is adopted in this research, does not attempt to locate universal truth or generalise theories that explain the MCSs. Otley and Berry (1994, p.50) argued that “it is fair to note that generalisation is not the prime concern of researchers using this approach.” Instead, the objective of using the case study approach in this study is to understand the existing MCSs in Libyan case studies industries within their developmental environment.

### **2.2.2 Data collection methods**

For this research study, data was collected from the Libyan Food, Paper and Construction Materials industries under research through interviews, document analysis and observation. Interviews with people could have been recorded on tape for later translation by researcher, but from the researcher’s experience, most of the Libyan interviewees were more likely to talk freely without the presence of a tape recorder. In qualitative research it is helpful to use multiple methods for data collection so as to enhance validity and reliability. The advantage of using multiple methods for data collection was the combination of the examination of the events and occurrence of the findings and evidences about the phenomenon being studied. In this study multiple methods of data collection were used to attempt to avoid ‘threats’ to validity and reliability. Research that has employed multiple methods has the ability to capture threats to the phenomena under investigation (Ferreira and Merchant, 1992; Yin, 1994). A brief summary of data collection methods is now given.



### 2.2.2.1 Interviews

Interviews are often thought to be the best way to collect data because in comparison with other data collection methods they enable the researcher to capture deeper thoughts, insights, problems, and opinions (Yin, 1994). If the researcher is going to answer simple questions then the questionnaire is preferred but when answers need to be explored and clarified, interviews give more flexibility than questionnaires. For this research semi-structured interviews were adopted in order to collect data about the phenomenon under study. The importance of the interview is noted in the following statement of Burgess (1982, p.107): “An interview is the opportunity for the researcher to probe deeply to uncover new clues, open up new dimensions of a problem and to secure vivid, accurate inclusive accounts that are based on personal experience”. Consideration will be given to the problem of managing the bias in interviewing people in the industrial sector. Sekaran (1992, p.193) referred the source of bias to errors or inaccuracies in the data collected. Sekaran goes on to say that bias can come from three sources:

- The interviewer: this bias is introduced when the interviewer misinterprets the interviewees’ responses.
- The interviewee: the participant introduces bias when he responds in a way which the participant thinks that the interviewer is expecting, and would like to hear.
- The situation: situational bias is introduced when the interviewee does not feel comfortable in answering the questions, so gives inaccurate answers or answers that are lacking in detail due to the constraints of time or discomfort with, for example, who is within hearing distance.

This researcher adopted a number of measures to attempt to avoid such bias:

- The researcher attempted to establish trust between the interviewer and the interviewees by making them aware of the objectives of the study (see also Bochner, 1980).



- Making the participants aware that their responses could be treated as strictly confidential.
- The researcher did not impose the questions, but encouraged the people in the factories to respond freely and openly in order to understand their perceptions, attitudes, and feelings about the MCSs in Food, Paper and Construction Materials industries.
- Most of the interviews with people took place at a time and place convenient for the interviewees to reduce the possibility of situational bias.

In a Libyan context, interviews are preferred for practical reasons: the postal service is very unreliable, so the response rate of any mail questionnaires will be very low or non-existent. Libyan people do not generally care for mailed questionnaires because they think there is no time to spend on answering questions, or that there is no urgency to reply. Hence, the completed questionnaires can take months to arrive or maybe in some cases never arrive. Furthermore, the postal questionnaire is an inappropriate method for data collection in the Libyan context for four further reasons:

- Companies had changed location, especially public ones (for political and economic objectives).
- At this research time, there is no postcode for most Libyan companies; hence indirect contact (mailed questionnaires) is impossible.
- Many Arab researchers have suffered from the low response rate of the postal questionnaire (Abd-Elsalam, 1999).
- During a short visit to the research site for two weeks the researcher conducted interviews and asked many people in the industrial sector about their preferred method for data collection. The result was that 90% of them said they preferred interviews to mail questionnaires.
- As a result of the low educational level among the People's and Congress Committees in the Food, Paper and Construction Materials factories, interviews were an appropriate method to explain the questions in order to avoid any misunderstanding and to gain people's co-operation when all they have to do is



talk. Sellitz (1966) stated that many people “are willing and able to co-operate in a study when all they have to do is talk.”

In the Libyan context, researchers need to be in the research field and to introduce themselves to the participants as great emphasis is placed upon personal contact. Consequently, interviews are an appropriate instrument for data collection in this research. In terms of who was interviewed, the researcher interviewed face to face most of the members of the People’s Committee and the Congress Committee, the heads of the departments, and accountants in the case study factories in order to gain an in-depth understanding of their opinions, suggestions, difficulties, and ways of managing and controlling their organisations. On a macro level, most of the key people in the Ministry of Industry, Ministry of Economy, Ministry of Finance, The General Privatisation Committee and the Ministry of Planning were interviewed. During the actual interviews a semi-structured interview approach was adopted and supplemented by open-ended discussion on topics raised both by the interviewer and the interviewee. All the interviews were written up immediately in order to analyse them.

#### **2.2.2.2 Document analysis**

Document analysis is the analysis of documents from the organisations to attempt to gain some extra data related to the phenomenon being studied. Documents can provide evidence about personalities and conflicts between the individuals (Brownell, 1995). Yin (1994) argued that documentary information is likely to be relevant to every case study topic. For this thesis, the documents considered in the enterprises studied included letters, as well as written reports of events and administrative documents such as production reports, budgets, the state decisions, progress reports, accounting statements (profit and loss accounts and balance sheet), other internal documents, and external formal studies or evaluations of the same topic. The importance of document information is one of triangulation, in order to corroborate and add to the evidence from other sources, thereby increasing validity (Yin, 1994).



The principal aim in considering the main documents in the Food, Paper and Construction Materials factories under research was to construct a solid background about the people, the nature of the activities and the rules in these companies; for conducting interviews, prior information about the people and their fieldwork was required. The procedures for obtaining documents from TBF were very stringent. For example, the researcher required a copy of the production reports from the accountant, but the accountant refused to provide these until the researcher had obtained permission from the Head of the Accounting Department and the Director of Financial and Administrative Affairs. This process was not because of administrative regulations but because the accountant was afraid of losing his job (the accountant was Sudanese).

#### **2.2.2.3 Observation**

Observation is a method of collecting data, which in this thesis involved watching the daily work process and other activities. Sekaran (1992, p.215) stated that “observation is the application of the sense of vision to gather information about people in their natural work environment and to record their behaviour.” Observation has been argued to be one of the best ways for people to develop their knowledge about the world in which they live (Stake, 1995). Furthermore, this researcher attempted to become a complementary part of the environment being studied so as to become closer to people participating in the case studies context and to understand the phenomenon being investigated from their experience, words and views.

### **2.3 Summary**

This chapter reviewed the main objective of this research: to explore and gain an in-depth understanding of the MCSs using Food, Paper and Construction Materials industries as case studies within their environmental developmental context. According to the nature of the research, interpretive methodology and qualitative methods were adopted as the best way of understanding the current MCSs in their organisational context. The interpretive approach is an appropriate way to establish why particular enterprises follow their particular present use of MCSs and what they are used for. Case



studies were utilised as multiple data sources (Yin, 1989). The case study approach was adopted to achieve the research objectives. Interviews, observation, and document analysis were used as data collection methods, which is known as the data ‘triangulation’ approach.



## **Chapter 3: Locating the analysis: review of some relevant prior literature**

### **3.0 Introduction**

The previous chapter focused on the methodology adopted and the methods for data collection from the research site (the Libyan private sector). This chapter aims to focus on the characteristics of studies of, and approaches to, management control and the role of accounting in the processes of socio-economic development in that country. The understanding of these studies and approaches is important in order to explore and understand the actual situation of the MCSs in the Libyan industrial sector, particularly in the Food, Paper and Construction Materials industries, which form the case studies of this research.

### **3.1 Traditional approach [Anthony's established model]**

It is generally agreed that Anthony's classification (1965) of management control activities into the three categories of strategic planning, management control and operational control has had a significant impact on the development of the theory of MCSs. However, it has been extensively criticised by many researchers recently (Lowe and Puxty, 1989; Otley, 1985; Laughlin, 1987). For instance, Otley (1985) argued that "strategic planning cannot be divorced from control, for effective control involves changing plans and objectives. Nor can operational control be kept separate from management control for its technological complexities impinge directly on the control process." Moreover, Anthony's definition of management control can be argued to be too narrow and restrictive. Machin (1983) criticised Anthony's reliance on management accounting as being the major vehicle through which management control could be exercised. Also, Lowe and Puxty (1989) stated that Anthony's definition narrowed down the scope of the subject, and lacked any awareness of the overall holistic nature of control. They further criticised Anthony's classification on a number of issues:



- It ignored the relationship between an organisation and its environment.
- It considered the control process as only a feedback process.
- It perceived planning as a separate process and not as a pre-control process.
- It lacks a holistic framework.

Furthermore, according to Anthony, the structure of management control is concerned with responsibility centres. Responsibility itself is a human concept, and as such can be seen to be a frame of control over people rather than control over an organisation. To understand control it can therefore be argued that it is necessary to understand the relationships between an organisation and its environment, as control over people within the organisation in such a restricted sense is not, arguably, control in a true sense. Anthony's paradigm further ignores the relationship between an organisation's goals and an individual's objectives. Anthony also neglects the societal context of an organisation, because, he ignores the fact that the members of an organisational coalition are also members of its society. Lowe and Puxty (1989, p.23) suggested that "the goals of the organisation cannot be considered in isolation from the context in which it exists ... [in the same way] the goals cannot be considered as decidable 'by' the organisation."

Lowe and Puxty also noted that the traditional approach does not consider the real structure of an organisation. To be precise, any organisation has a real structure, and this structure is not necessarily the one that appears on the organisation chart, rather, the formal structure is a 'wished-for' structure on the part of certain organisation designers. Furthermore, an organisation structure (both real and formal) is changeable, as is any other circumstance (Lowe & Puxty, 1989).

For this research, the traditional approach is arguably inappropriate, because the main objective of this study is to understand the nature of MCSs in the Libyan Food, Paper and Construction Materials industries within their own developmental environment. Thus, in order to meet the research objectives, an approach that covers and considers the relationships between the organisations and their environment is required. This study will use a systems approach for the reasons outlined in the next section.



### 3.2 Systems ideas

Thompson (1967) introduced the closed system and the open system by basing his theories on an interpretation of Gouldner's (1959) model. Ansari (1981, p.34) summarised the differences between the two system types thus: "the closed systems strategy is aimed more at the autonomous behaviour of a system's components whereas the open systems strategy aims to study the ways in which these components are integrated and the behaviour of the resulting whole". Closed system approaches are appropriate when directing attention to searching for 'rational' decision behaviour within the organisation (Thompson, 1967). However, they often tend to be inaccurate representations of reality, because they exclude many complex interactions between the sub-parts of the organisation, and isolate the organisation from problems of change and uncertainty in the external environment (Thompson, 1967, p.2). An alternative approach for organisational analysis has been derived from general systems research and it is one that directs attention at the complex interactions between parts of the organisation and between the organisation and its external environment. In this approach, known as the systems approach, every part of the organisation is considered as an interdependent part, each contributing and receiving something from the whole. The organisation as a whole interacts with its environment by receiving its needs from the latter as input and exchanges the outputs with the environment in order to provide additional resources. Katz and Kahn (1966) described the interaction between the organisation and its environment as "the energetic input into the system, the transformation of energies within the system, and the resulting product or energetic output."

Berry *et al.* (1995, p.13) argued that systems approaches consist of two types of systems: 'soft' and 'hard'. The former tends to relate to systems that include human beings, where objectives are vague and ambiguous, decision processes are ill-defined and possibly irrational and where at best only qualitative measurements of performance exist. The latter tends to relate to physical systems having relatively clear objectives and decision processes, with quantitative measurements of performance. It is apparent from the distinction above that soft systems approaches will have most to offer the study of



management control. The application of a systems approach to an organisation could be divided into two parts: first, the relationship between the organisation and its environment and second, the interaction between the organisation's subsystems.

#### □ **The external environment**

The system consists of a set of elements that are actively interrelated and operated in some sense as a total or whole unit, while the system's environment is seen as a set of elements that interact with the system. The environmental factors are usually separated into general and specific categories; the general environment refers to the factors that affect every aspect of life (such as the economic sanctions, the state and employment), and the specific environment refers to the factors that directly affect the organisation in day-to-day processes (such as budgeting and pricing). Accounting systems that provide information on the external environment often identify the relevant environment as those aspects that directly affect decision and organisational processes, and over which managers have a degree of control. In order to obtain a solid understanding of the relevant factors in the systems it is necessary to understand broadly the interaction between the organisation and its environment. An open system approach provides a way of thinking that directs attention toward achieving this objective (Chenhall *et al.*, 1981).

#### □ **Internal subsystems**

The identification of the sub-parts of the organisation may follow many approaches: one effective approach was developed by Parsons (1960). In his approach the organisation is divided into three subsystems: a technical subsystem (production), an operational subsystem (maintenance and managerial) and institutional subsystems (production support, adaptive and institutional). Identification of subsystems and the way in which they interrelate is an important criterion for understanding the relationships between the organisation and its environment and also between its subsystems. An identification of the different subsystems may reveal the different information needs for the decision making and control functions of managers. Lowe and Tinker (1977) introduced a framework for the internal structure of the organisation that consists of three



subsystems: a decision and control subsystem; a financial funds subsystem and an operating (physical transformations) subsystem (see Chapter 1).

A general systems viewpoint is concerned with identifying the whole of the system to which the problem relates and it thus seeks to avoid taking that system apart in a manner which would result in the loss of essential characteristics of the problem. Berry, *et al.* (1995, pp.14-15) stated that GST and cybernetics can contribute to the study of MCS in a number of ways. First, the system's analysis of the management control can be holistic rather than reductionist in approach. Second, by using the systems approach, the 'real-world' problems of management control could be explained and understood. Third, the concepts developed in GST and cybernetics are used to develop the theory of management control. Finally, a systems approach such as the open systems in organisation theory has been used in different areas related to MCSs. Thus, the systems approach offers a method of studying management control that has the potential to recognise at least some of the fundamental problems. As this study is taking place in a developing country (Libya), it is necessary to note some characteristics of developing countries in general in order to obtain a broad understanding of the world of which Libya is a part. The Libyan environment in detail will be the subject of Chapter 4.

### **3.3 Developing Countries: Characteristics and management control**

Before introducing the characteristics of developing countries it is necessary to explain the meaning of 'developing countries' and the other phrases such as 'third world' and 'underdeveloped countries'. Although the literature does not contain any exact definitions of the above phrases, these phrases are used when referring to the countries that do not belong to the Western or the Eastern World. Wallace (1990, p.4) suggested that developing countries are "different in terms of GNP, population, culture, degree of literacy, economic and political systems" from developed countries. The developing countries are typically African, Latin American, Asian, Middle Eastern, and South Pacific; these countries were subjected to long periods of colonisation by developed countries, and most of them gained their independence in the late 1950s when de-colonisation became a global phenomenon (Wallace, 1990, p.3). Some criteria have



been used in terms of defining developing countries. For example, the United Nations, (1951, p.3) in its conference about development, used per capita income and defined developing countries as “countries in which per capita real income is low when compared with per capita real income of the USA, Canada, Australia and Western Europe.” This criterion has been criticised by the argument that “in modern thinking, higher per capita income can not be the only criterion to judge the level of development” (Talukdar, 1978, p.18). For example, Kuwait in 1973-74 had double the income level per capita of the United States, yet was still regarded as being a developing country (Talukdar, 1978).

Developing countries are a heterogeneous group (Perara, 1989, p.149). They may differ in terms of their geographical size, their level and rate of economic, social and political development, their political and economic systems, natural resources, population, culture and level of literacy. They are completely different from developed countries and may need different ways to develop (Wallace, 1990; Chandler and Holzer, 1984). Also, a common characteristic of most poor nations is that the available natural and human resources are not used to good advantage (Scott, 1967). Generally, most developing countries share the following attributes:

- They have unbalanced distribution of income and wealth, exporting agricultural and mineral products in very limited ways.
- Domestic industries are at varying stages of development; most of these industries are facing serious balance of payment problems because their demand for imported goods far exceeds the foreign exchange earnings from their exports.

In the case of Libya the decision-makers have supported the industrial sector to overcome these problems through a dependence on local raw materials and an encouragement of all kinds of activities in this area. Article 2 in the industrial development plan 2001-2005 supports this point, by focusing on replacing the production strategy, which was based on the wide distribution of different industrial activities throughout the whole country, to concentrate on industries that are based on local materials and have the ability to develop as well as to grow.



Briston (1984) concluded there were three major factors that have become the concern of all developing countries:

- The will to generate foreign exchange reserves.
- The need to increase the local content of industrial production, which depends on local raw materials and the training of the local people to solve the unemployment problem and to take over jobs previously done by foreign workers. This objective is one of the reasons for choosing the Libyan Construction Materials sector for the topic of this research as it is dependent on local raw materials.
- The urgent desire for economic independence resulting in an increasing demand for international companies operating in these countries to provide information about technology received from parent companies and the extent of local participation in their equities.

Accounting systems in developing countries have been widely criticised by many researchers as being unable to establish coherent information systems to meet the needs of their countries. Briston (1978) stated that “so far no developing country has been able to construct a system of accounting designed primarily to meet its own information needs.” Enthoven (1973) described the accounting system in developing countries thus: “Ironically, most developing nations have chosen to engage in the erroneous and often regrettable practice of ‘importing’ accounting systems from developed nations.” Most of the accounting systems in developing nations have been borrowed from developed countries. Samuels and Oliga (1982, p.69) suggested that “an examination of the sources of existing accounting systems were for the most part either imposed by powerful foreign investors or extended from the home to the host countries through the influence of multinational companies, foreign aid, and education.” The most important method for transferring accounting systems from developed countries to developing countries was colonisation (Hove, 1982), and Libya (see section 3.4) has indeed adopted many accounting systems as a result of British, American, and Italian colonisation.



Mirghani (1982, p.57) described the role of accounting in developing nations thus: “in the majority of developing countries, there is a lack of awareness of the potentially significant role that accounting could play in the economic development process.” Scott (1967) concluded that the accounting enterprise in developing nations does not provide the required information to the same degree as is the case in advanced nations. Enthoven (1977) finds that significant versions of accounting such as management accounting and government accounting receive less attention in developing countries. Management accounting as practised in developed countries is rarely ever practised in developing countries (Holzer, 1984).

### **3.4 Management Control and Management Accounting functions in developing countries**

Wallace (1990, p.4) stated that accounting research in developing countries “has grown from an early normative interest in the contribution of accounting to the development process to the empirical study of different ways by which the accounting profession, education and practice have grown in the developing countries.” It was only from the 1960s onwards that the role of accounting in economic development has gained a high level of attention from accounting researchers (Taylor and Turley 1986, p.90). Enthoven (1981) argued that there was a need to achieve relevant accounting education in terms of economic development. Foroughi (1981) described the importance of the role of accounting in economic and industrial development by noting that:

“[A]ccounting can help the economic and industrial development processes of developing countries in two ways: a) by leading and guiding the investing parties to invest in useful, profitable and productive projects, and b) by helping the management of the industrial and business enterprises to plan for the efficient utilization of development capital” (Foroughi, 1981, p.182).

It can therefore be concluded that accounting plays an essential role in economic development and that this role will continue in the future. Hopwood *et al.* (1990) stated that:



“Accounting is, has been, and no doubt will continue to be, intimately involved with the development of the economy as a whole. As one of the most important forms of operational economic calculation, accounting has not only reflected prevailing economic conditions but has also played a significant role in enabling the implementation of different strategies for the management of both the national economy and particular enterprises within it” (Hopwood *et al.*, 1990, p.39).

Accounting should be seen as part of the economy, as it goes hand in hand with development plans. Libya, as a developing country, has many weaknesses in its economy and its accounting system. Wallace (1990, p.4) argued that accounting in developing countries is still a “nascent” field for study and noted that in developing countries there is a belief that accounting plays a vital role in the achievement of economic growth and there is an urgent need for a deeper understanding of accounting systems in developing countries.

#### **3.4.1 Accounting, development planning and resource allocation**

It is worthwhile noting that on one hand, the wants and needs of human beings are unlimited, yet on the other hand, the resources required to satisfy these needs and wants are in very limited supply. Therefore, the achievement and improvement of economic development plans depend on utilising a country’s scarce economic resources. The UN report (1965, p.12) noted that “it is an integrated task of planning to achieve the best possible use of scarce resources for economic development.” In developing countries, development planning is an important tool for resource allocation, owing to the failure of the market to provide suitable guidelines. Belkaoui (1985) argued that:

“Development planning is generally accepted as essential to the economic development of the developing and even some of the developed countries. The need for planning in the developing countries is accentuated by the ‘failure’ of the market in those countries to price factors of production correctly” (Belkaoui, 1985, p.335).

The proposal and drafting of the general or specific plan is an important step in the development process and controlling and assessing this plan is the most important step in identifying the progress of the plan and making the necessary changes to maintain its



existence. The controlling and checking of development plans should be carried out by the management and personnel in the companies. Any comments, corrections, and changes in the plan are regarded as important feedback information so as to orient the development processes to accomplish the output objectives. Gordon (1974, p.88) suggested that the essential role of feedback information is to control the system's output. According to Samuels's (1990) review of accounting in developing countries, the major problems developing countries have confronted and the accounting statements that could provide relevant information to understand them are shown in Table 3.1:

Table 3.1: Major problems of developing countries and types of accounting statement that would ostensibly aid their resolution.

	Problems	Relevant accounting statement
1	Economic Growth	a- Profit and Loss account b- Balance sheet (with notes) based on inflation adjusted figures
2	Unemployment	Employment report
3	Balance of payment	Statement of transactions in foreign currency
4	Income/ wealth distribution	a- Adapted value added statement b- Analysis of shareholders
5	Level of technology	Education/ training report
6	Regional imbalances	a- Regional flow of funds statements b- Regional distribution of assets
7	Safety/security	Employment report
8	Impact of environment	Special report
9	Corruption	Audit report

Source: Samuels (1990, p.80)

### 3.4.3 Management control and management accounting and their environment

Developing countries as any other countries need effective systems, systems that are able to provide the necessary information for the decision-makers for the planning and control of their economies. Furthermore, accounting systems are systems that play a



vital role in improving the quality of the development plans and the future decisions. Although the relationship between management accounting and environment is a field that has been widely examined, this has not been done in the context of small and medium sized enterprises<sup>7</sup> (Greenhalgh, 2000). A few studies have been conducted in the context of developing countries in the area of management control. For instance, Hoque *et al.* (1994) conducted an interpretive study on a public sector company in order to understand the actual situation of accounting and budgeting systems and the impact of the environmental factors on these systems by using a case study approach. The main finding of their study was that environmental factors played a vital role in shaping the organisation's control systems. Furthermore, Macintosh and Daft (1987) investigated the relationship between the organisational characteristics of departments of public organisations and three elements in a package of management control. They concluded that the management accounting system as one element of the management control package was studied in isolation from other characteristics of the total organisation and this was why researchers still have a narrow understanding of its function. Alam (1997) investigated the budgetary process in the uncertain context of Bangladesh. Alam concluded that uncertainty in the task environment had a considerable impact on the budgetary process in Bangladeshi state-owned organisations.

Anthony (1989) described the current state of management accounting practice as very poor: "Information about management accounting practice is abysmally poor and almost all information is anecdotal." Yet, Drury and Tayles (1995) stated that in the past decade there had been an increase of perception and emphasis of management accounting practice. Marriott and Marriott (2000) also emphasised that the limited quantity of information obtained by owners/managers from their accountants clearly affected their need for management accounting services in the future. In addition, Raymond and Magnenat-Thalman, 1982; Holmes and Nicholls, 1989; Nayak and Greenfield, 1994; Lybaert, 1998 all noted that the level of positive performance of small/medium enterprises depended on the quality of management accounting information (hereafter, MAI) available to the management of these enterprises for the control of their day-to-day activities. The management control and management

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<sup>7</sup> The context of the research.



accounting found in small/medium enterprises are derived from managerial needs and demands in order to direct their organisations to achieve their objectives.

Yet Briston (1990) suggested that in most developing countries MCSs are neglected. As developing countries are a heterorganic group, the accounting and control needs in third world countries differ greatly from country to country (Peasnell, 1993, p.2). It is worthwhile noting that all the above studies were conducted in developing countries and this study has been conducted in Libya, which although being a developing country, has a unique situation in terms of economic, social, political and cultural aspects (see Chapter 4). Accordingly, many of these studies can be considered as only partially relevant to the Libyan environment, so focusing on studies conducted in the Libyan environment is particularly useful in order to understand and inform the present study (see section 3.5).

### **3.5 Management control and management accounting in the Libyan context**

This study is regarded as the first study to have focused on the MCSs in the Libyan private sector as all the previous studies in the area of management control and management accounting were focused on public sector organisations. This is understandable given the Libyan economic context in which the public sector has dominated, especially within the two decades 1969-1988. Yet, since 1988, the private sector has played a vital role in contributing to the development of the Libyan economy after the perceived failure of the public sector to achieve its developmental objectives (see Development Plan 2001-2005). This study is the first study to have focused on this so far neglected sector by a Libyan researcher and it aims to gain a better understanding of MCSs in this sector within its developmental environment. Furthermore, in the area of management control and management accounting very few studies have been conducted in the Libyan public sector. Indeed, this researcher has managed to find only two studies in the literature regarding the area of management control in Libya. These will be summarised here.



The first is by Bait-Elmal, (2000) who conducted an interpretive study thematised around systems ideas in a Libyan public sector organisation. He was attempting to understand the functions of management control in the Libyan public sector by using a single case study approach. The study being written by this researcher differs from that of Bait-Elmal in a number of ways. First, although he was concerned to understand the MCSs in the Libyan public sector using a case study approach, the case study he used was the National Mill Company for Flour and Animal Fodder, a company 100% state owned. In order to achieve the study's aims, Burrell and Morgan's framework (1979) was used as a means to accomplish the research objectives. An interpretive methodology was also adopted as the best way to understand the dynamics of the MCSs and the richness of the organisational functions. A single case study from the Libyan public sector was selected for that study. The main objective of the state was the provision of the flour and animal fodder, and this objective was reflected in the state's aims and the management of the company was forced to accept this. These personnel had no role in the establishment of the company objectives. Consequently, the outcome of the company activities meant nothing to them, as they had a monthly salary, which was secured by the state. Bait-Elmal concluded, therefore, that the company's objectives had little influence on the employees as a means of managing and controlling the company's day-to-day affairs.

This present study, however, focuses instead on the Libyan private sector, in order to gain an in-depth understanding of the MCSs in those Libyan organisations that were public companies and have now become private ones. In the private sector, the organisation's objectives play a vital role in managing and controlling activities. Privatisation has given personnel a chance to be owners and to work for themselves and is considered as a motive for the employees to achieve the development objectives for both the factory and the country. This study paid great attention to the industrial development plan 2001-2005, which consisted of many changes and new emphases in the Libyan economy (see Chapter 5). Three different industrial sectors were chosen for this study, in order to gain a deeper and better understanding of the actual situation of the MCSs in these sectors and the influence of the environmental factors on their effectiveness. Using three case studies instead of one was done with the aim of



enhancing the findings and richness of arguments of this research. Yin (2003, p. 133) stated that “having more than two cases could strengthen the findings”.

The second of the two other studies was by Gzema (1999) who also conducted a study on management control in developing countries. This study focused on the oil industry in Libya and used an old institutional economics and a case study approach in order to attempt to gain a better understanding of management control practices in Libyan public companies. As in the Bait-Elmal study, the focus in Gzema’s study was also on the Libyan public sector. An oil company was the basis of the case study of his research, aiming to gain a better understanding of the management control functions in the Libyan oil companies, which are completely state-owned. The old institutional economics was the chosen methodology, Gzema arguing that this methodology had the ability to offer a better understanding of management control practices in Libyan public companies in general, and in Libyan oil companies in particular. In comparison to Gzema’s study the present study differs in many ways. The focus of this study is on the Libyan private sector, which is regarded as a different context from the public sector. The case study approach and systems ideas are used in this research in order to gain in-depth understanding of the actual situation of the MCSs in the Libyan private organisations. By using systems ideas, considerable attention was paid to the environmental factors that influence the MCSs in these companies and three case studies have been used instead of one in order to achieve the objectives of this research. Many changes in the Libyan economy (such as the privatisation process) have been taken into account in the case studies.

Neither of these two previous studies has been concerned with the economic and social development plan 2001-2005, which has led to many changes and different focuses, especially in the private industrial sector. The structure and management in the private factories has some significant differences from public companies, such as the existence of a Productive Congress and Congress Committee in the private factories. The Productive Congress operates with state authority in the factory (see Chapters 6, 7 and 8).



It can be concluded that the above studies are different from this research in two respects: first, this study focuses on the private sector as a site of research, which may differ from the public sector, especially in terms of objectives, structure and environment relations. Puxty (1993, p.70) argued that replicability in social situations is very difficult, as every social situation is unique if only because any situation can happen in a different place and at a different time from the other situations. It is unique, in that the particular people involved in the particular situation will interpret it in a particular way. Consequently, not only will unique understanding lead to a unique definition of a situation, but also one needs to remember that no other situation can be quite the same. Hence, a replication of the event can never lead to a replication of the factors, precisely because they were generated by the unique circumstances of that particular set of observations. Second, three case studies – not one – were chosen (Food, Paper and Construction Materials industries) in order to explore and gain an in-depth understanding of the MCSs in the Libyan private sector. Systems ideas and an interpretive approach were adopted in order to be close to people to understand from their own words and experiences the phenomenon under investigation. Systems ideas were seen as appropriate way to understand the social phenomenon in a holistic system instead of focusing on a part of it. A case study approach was also adopted in order to enhance the holistic understanding of the management control functions (see Chapters 6, 7 and 8).

### **3.6 Summary**

Most plans for development reveal a strong desire on the part of the government to increase industry's contribution to the economy, and it is said that development of both management and financial accounting has become widespread. Government planners, managers and owners need information on the activities of the business enterprises involved in the industrialization process and a developed management and financial accounting system is required for future development in order to provide information for the decision-makers.



The Libyan accounting system has many characteristics; first, the western-style of accounting was imposed in Libya without any balanced consideration of Libyan environmental needs. Indeed, one of the goals of this research is to understand the influence of such external factors on the MCSs and accounting system in private sector organisations, in particular in the Food, Paper and Construction Materials industries (see Chapter 5). Second, deficiencies exist in the present Libyan accounting system, (a common characteristic of accounting systems in developing countries is that their accounting systems are deficient (Wallace, 1990)). The present review shows that there are many weaknesses in the Libyan accounting system: first, a lack of any management control concept, which is the area of this research (i.e. mainly MCSs). Second, Libya has inadequate, untimely aspects of financial accountancy, incomplete, inaccurate reports and also a notable lack of skilled accountants, who also have inefficient management control information. Third, owing to the weakness of their accounting education, developing countries are not aware of the value of a good accounting education system and how it can help develop their environments (Enthoven, 1983, p.110). From a close look at Libyan accounting education it appears that there are some accounting subjects that have been ignored, such as management control, management accounting and governmental accounting, all of which play a vital role in modern economies. Indeed, management control and management accounting are greatly neglected in Libyan accounting education, their proportion being just 5.8% of the total hours in accounting courses. Finally, most sectors in the country do not recognise the importance of accounting and the information it provides to support the economic development process. A strong accounting system in Libya does not exist and there is only a weak link between the economy and accounting education. Libya as a developing country, has rapid economic growth and urgently needs to rebuild a strong accounting education system to support its accounting system by providing skilled accountants, mainly in management control and management accounting, to meet Libyan management needs.

Having in mind the systems idea, the interpretive approach, case study approach and Yin's call (2003) to rely on theoretical propositions as a guide when conducting case studies, the research, as mentioned earlier, will focus on specific themes of MCSs in



order to achieve the research objectives. These themes include organisational objectives and structure, management, accounting system, budgeting system, reward system and cost and pricing systems. The research was not constrained by these themes but remained open to any new themes that might appear during the empirical work process (see Chapters 6, 7 and 8).



## **Chapter 4: The Context of Libyan Business Activity**

### **4.0 Introduction**

The previous chapter addressed the relevant prior literature to this research. The objective of this chapter is to provide a wider description of the economic, political and social factors in the context of the research site (the Libyan Food, Paper and Construction Materials industries under study), in order to understand the relationships between the external factors and the organisational processes (MCSs). To achieve this purpose, this chapter is organised as follows: section 4.1 discusses the social, cultural, economic and political environment; section 4.2 presents the development within a Libyan context; section 4.3 provides the reasons for the selection of Tripoli Municipality and section 4.4 is a summary of the chapter.

### **4.1 Social, cultural, political and economic context**

*“The nature of the organisation’s relation to its environment and of its goals cannot be understood except in the context of its relations with its wider social context”* (Lowe and Puxty, 1989, p.22).

Throughout history it is known that society and the practice of accounting have run in the same direction. Political, economic, legal, technological and sociological factors have influenced the development of accounting and all these factors play a significant role in shaping the design of an accounting system. Studying and understanding the accounting system required an understanding of the environment of accounting in any country. As Alhashim and Arpan (1988, p.9) noted: “To understand properly any country’s accounting system, one must understand the country’s environment. This situation is true even for properly understanding the accounting of one’s own country.” The purpose of the following sections is therefore to provide information about the Libyan case study industries in order to gain in-depth understanding of the influence of the external environment on shaping the MCSs in these industries.



#### 4.1.1 History of Libyan society

Libya is a developing country located in the north of Africa with an area of 1,759,540 square kilometres (Africa development bank, 1995) and it is one of the largest countries in Africa. It is nearly one-half the size of Europe or one quarter of the area of the United States of America. Around 90% of the land area is desert and the rest of it is used for grazing; only 1% is arable land (United Nation, 1991, pp.34-35). Libya also has sandy areas and two areas of hills and mountains rising to a maximum of 3,000 feet above sea level, with mountain Jabel Nafosa in the north-west and mountain Jabel Alakder in the north-east.

Libya is characterised by a mild climate prevailing over its various regions. In Tripoli (the capital city) winters are usually rainy and cool, and summers are hot and windy. The climate is always mild as a result of its being located near the Mediterranean Sea. The country has a long coastline on the Mediterranean Sea (around 1,900 kilometres), and is also bordered by a number of countries; Algeria, Egypt, Sudan, Chad, Niger and Tunisia (see Figure 4.1). The state religion is Islam and the official language is Arabic: English and Italian are used for trade. Tripoli's municipality<sup>8</sup> has an important location on the Mediterranean Sea. This location gives the city priority to become the centre of population and of any development activities. This reason and others (in next sections) encouraged this researcher to choose the Tripoli municipality for the empirical study of this research in order to gain a better understanding of the existent MCSs in the Food, Paper and Construction Materials industries (see section 4.3). Tribe/family units function as the most important social networks in Libyan society. Mogherbi (1998, pp.56-74) described Libyan society thus: "Family, tribal and regional affiliations are more important than class structure in influencing the social and political interaction in Libyan society ... tribal affiliation is a most important factor in determining the choice of people's committee members at their different level." In Libyan society the deeds of individuals bring collective fame or shame to the family and tribe. Consequently, a good or bad reputation of family and tribe is of critical importance on the lives of people socially, politically and economically. An understanding of the influence of Libyan

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<sup>8</sup> The research region, which could be divided into two municipalities in the future.



society’s structure on the MCSs in the case studies industries is therefore fundamental to the aims of this research.

Figure 4.1: Map of Libya





#### **4.1.1.1 Islam and Libyan society**

The most powerful influence on Libyan society is that exercised by religion, which plays an important role in Libyan society. Plamer and Omar (1982, p.11) pointed out the role of the religion, saying that it “significantly affects the structure, values, and attitudes of Libyan society. It is [the] primary unit of loyalty and identity.” Since 643 A.D Islam has been the basic code of life in Libyan society, remaining so even during the Italian occupation from 1911 to 1943. Islam comprises a comprehensive structure of ethics, politics, social structure, arts and science. Ali (1967, p.138) summarised the essence of the ethical principles in Islam as: “(1) a belief in the unity, immateriality, power, mercy, and supreme love of the Creator; (2) charity and brotherhood among mankind; (3) subjugation of the passions; (4) the outpouring of a grateful heart to the Giver of all good; and (5) accountability for human actions in another existence.”

According to Ali (1967), the social concepts of the Koran are based on Islamic social justice and the equality of all people. Hence, under Islamic law, people are equal in the eyes of the law. In terms of politics, it consecrates the principles of self-government (Ali, 1967). Since 1969, Islamic and socialist ideas have been the only approaches used in order to change the Libyan economic structure, and these changes were to change the nature of property ownership in Libya. In Islam, property is owned by God and ownership rights are limited by inheritance rules, prohibition of usury, as well as obligation to the Zakat<sup>9</sup>, a wealth tax. People working in Food, Paper and Construction Materials activities as a part of Libyan society seek to realise their profit and wealth to pay Zakat. To do this, information about the activities of the factories must be provided by the factories’ management. Under the Islamic inheritance system, the individual has the right to one-third of his property, while two thirds can be inherited by the person’s family: sons, daughters and other family members. According to Islamic law all the person’s sons and daughters have the right to inherit their parents’ property, but sons

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<sup>9</sup> Wealthy Muslims have to pay 2.5% of their liquidity as Zakat every year.



should take twice as much as daughters. A wife also has the right to one-quarter of her husband's property after his death. If the husband has no children, his parents each inherit one sixth of his property. The husband has the right to one quarter of his wife's property after her death, and the remainder goes to the children unless the mother-in-law and father-in-law are alive (Wilson, 1983). All these relations and outcomes affect the research case studies activities especially when the producer<sup>10</sup> or worker dies. Article 11 from the Food factory's ownership contract suggests a limited role for inheritors: "In the case of a member passing away the factory will continue in operation between the other members and inheritors are not allowed to seek the desolation of the factory." (see Appendix A)

The Koran admits the rights of the private ownership of property; in the same way, this private ownership should serve a social and religious function. Wilson (1983, p.122) argued that "the reward of property can not be earned without the owner utilising these resources in a socially beneficial way. Property is not to be accumulated as an end in itself, but as a means of serving society as a whole." Islam does not forbid any economic activities such as trading and production for the market; rather, Islam permits trading. Yet it forbids usury, which is nowadays interpreted as the interest on loans, and this prohibition undoubtedly affects the financial capability of Food, Paper and Construction Materials activities. Understanding the MCSs of these activities and the influence of religion on the implementation of these systems is one of the interests of this research.

#### **4.1.1.2 Other social forces**

Arabic is the official language in Libya. Therefore, the legislation requires that all signs and documents should be in the Arabic language. In addition, Islam is the only religion practised in Libya, where it means peace, submission and obedience and provides both a spiritual guide for individuals and the basic source for all governmental rules and policies. However, since the Libyan revolution in 1969, although Islam has been the state religion, other religious groups have also been permitted to practise their religions

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<sup>10</sup> An employee in the Libyan privatised sector is called a producer.



within the country. Most of Libyan society consists of tribes who had a strong connection between each other until the discovery of oil, which influenced all social life, when new social elements emerged in the society. Many Libyans were introduced to new ways to life and many chances were created for people to improve their lives, especially women. Women joined most of the social activities outside their homes and as a result of this change, the rate of illiteracy was reduced and people became more independent, not just relying on the aid of their families. It can be concluded that understanding the influence of the Libyan environmental factors on shaping the MCSs in the Libyan private sector in general, and the case study industries in particular, is another of the main interests of this research.

#### **4.1.2 Formal political environment today**

Libya has experienced many different eras of different types of colonisation and each era has affected the political experience and the political environment in Libya. Libya is a name that was given by the Greeks who used 'Libya' to identify the area engaged by the 'Berbers'; Libya derived from the name of a single Berber tribe. Libya's very important location in the middle of the Mediterranean Sea gives the country a role as naturally strong link between Europe and central Africa, as well as between the Middle East and the North west of Africa. Libya was independent for around 300 years in the period from 900 BC to 1200 BC. Prior to this, Libya was invaded by numerous armies: the Phoenicians, the Greeks, the Romans, the Vandals, the Byzantine Empire and the Spanish (Mcguire, 1964; Farley, 1971; Nyrop, 1973; Fisher, 1985).

After the Spanish invasions (1530-1550), the first major political transformation in Libyan history was when the country was surrounded by the Arabs, who captured Tripoli in 643 AD. Libya now had a new identity far from the European world and closer to the culture and influence of Arab and Islam (Mcguire, 1964; Nyrop, 1973). The two components influencing Libyan culture during the period of Arabian dominance were the Muslim religion and the Arabic language. These components led to Libya becoming a more homogenous country (Farley, 1971, p.44).



On December 24, 1951, Libya became an independent state. There were two important developments that the new state undertook: the first was accepting the Arabic language as the official language; the second was forging the close link with Western Europe. The state faced some economic difficulties and the main problem was finding enough funds to meet the expenses and to pay for what was needed to improve the country. Since this time of independence many political changes have affected the Libyan people and their lifestyle. It is of great importance for this research to understand these changes in order to achieve one of the research objectives: the objective to understand the political influence on the MCSs in the present case studies industries.

September 1969<sup>11</sup> marked the beginning of an intrinsic change over all the Libyan economy in the form of a new stage of Libyan revolution. A group of about seventy young army officers and enlisted men, mostly assigned to the Signal Corp, seized control of the government and abolished the Libyan monarchy to declare the Libyan Arab Republic, Arab Nationalism being the main driving force of the revolution. The revolutionary command council (RCC) under the leadership of Mummer al Qaddafi took direct control of all the authorities and announced the creation of the new Libyan political system. The coup was then launched at all the Libyan regions, Army units gave their support to the coup and within a few days military control was firmly established in the main city of Tripoli and elsewhere throughout the country. Armed police and security forces who were thought to be loyal to the monarchy offered no resistance and consequently, the revolution was quiet and successful because there were no enemies and only a few arrests; no fighting or deaths were reported. Internally there were strict laws requiring Libyan people to control all businesses and all UK and US military bases established on Libyan land. The RCC insisted the personnel from these bases to leave the country as soon as possible and all the UK and US military personnel left Libya in March and June 1970 respectively.

In April 1973 a new revolution, the people's revolution in Libya, aimed to discover all the factors which prevented the achievement of the revolution's objectives in 1969; the

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<sup>11</sup> Libyan revolution took place in 1<sup>st</sup> of September 1969.



people's revolution motivated all citizens in all cities, villages, towns, schools and colleges to construct committees in order to implement the following:

1. nullification of all existing laws;
2. a purge of every factor against the march of the revolution;
3. distribution of weapons to the people who believed in the principles of the first of September revolution;
4. revolutionary modification of the administration through the changing of unqualified administrators and the selection of new ones;
5. a cultural revolution should take place including burning of all the important misleading books to give an opportunity for real human thoughts in the holy book of Islam.

The political development in Libya introduced a new type of democracy by the declaration of the establishment of the Authority of the people (Al-fajr Al-jadaed daily, 1977, pp.1-2). According to this declaration, direct democracy became the political system in Libya, and Libyans exercised their authority through Popular Congresses, Popular Committees, and Professional Unions. All three sections gathered to make the General People's Congress, and all Libyan citizens represented themselves when the General People's Congress met once a year to discuss and decide upon the policies of the country. The General People's Congress has four members in its general secretariat, headed by the secretary general who is the head of the state. The General people's Congress has the right to change the General Popular Committee and its president (see Figure 4.2) at any time. These political changes affected the industrial sector because all the industrial factories changed and became managed and controlled by People's Committees and Congress Committees elected by workers. The Food, Paper and Construction Materials industries reorganised their management to People's Committees (see Chapter 5). In order to understand how the People's Committees now manage and control these industries and why they operated the management and control systems in the ways that they do it is necessary to understand the political structure of the country.



The declaration of March 1977 also changed the name of the country to ‘The Socialist People’s Libyan Arab Jamahiriyya’. Jamahiriyya is an invented word in the political context, which means “people’s power” or the “state of the masses”. Article 3 in the Declaration (March 1977) described the People’s Authority thus: “the people’s direct democracy is the basis of the political system in the Socialist People’s Libyan Arab Jamahiriyya, where the authority is in the hands of people alone. The people exercise their authority through the people’s congresses, the people’s committees and the professional unions. The authority of the people is comprised of people’s congresses, committees, professional unions and general people’s congress.” The structure of the people’s authority system is divided into five parts:

- **The Basic People’s Congresses:**  
According to article 3 in the declaration, all people are allocated to Basic People’s Congresses on the basis of their place of residence. All citizens must register as members in the Basic People’s Congresses in their areas. Every Basic People’s Congress chooses a committee to lead the Congress from its members.
- **People’s Committees (PCs):**  
These Committees, which are chosen from the Basic People’s Congresses, are responsible to their Congresses. The membership term on the People’s Committee is limited to three years.
- **The Unions and Professional Associations:**  
All citizens who are members in the Popular Congresses belong professionally to ‘categories’. People can organise themselves into unions and professional associations. The main objective of these unions is to defend the professional rights of their members.
- **General People’s Committee:**  
This committee is responsible for the control and achievement of all the policies and plans of the state. This committee consists of five ministries (for more details see Figure 2.2).
- **General People’s Congress (GPC)[Parliament]:**  
This is the highest political authority of government in the country. It is the national conference of the People’s Congresses, People’s Committees and



Professional Unions. Vandewalle (1998) described the changes of the political and economic systems during the period of the 1970s as follows: “Economically and politically, the country had been thoroughly transformed by the end of the revolutionary decade (1973-1982): the state institutions had been put directly into the hands of people through a system of political congresses and committees ... The creation of this congress-and-committee system closely dovetailed with the ideological and political inclination of the regime.” Details about the political system in Libya are set out in the first part of the Green Book<sup>12</sup>. However, in September 1988 the government proposed an increase in the privatisation programme and a decision was taken to make Libya an open market to all private activities in complete freedom (Fisher, 1990). According to this ideology (privatisation) most public Food, Paper and Construction Materials factories were privatized and their ownership transferred to their employees in 1988 (see Chapter 5).

During the 1990s many modifications to the political structure of the country took place and the most important act in this period was that some authorities came down to the mezzo level of the general structure, as a step towards reducing centralisation. The General People’s Congress of Libya (GPGL) was still the top authority in the country and responsible for the issuing of laws, rules and the general policy of the state. The General People’s Committee of Libya (GPCL) was responsible for achieving the objectives of the state and implementing the rules by issuing procedures, which facilitated the accomplishment of this mission. Furthermore, in the new structural formation, the GPCL consists of five general committees: the Foreign Committee, the Public Works Committee, the Finance Committee, the African Committee and the National Security Committee. The GPCL with its committees has a direct connection with the mezzo level of the general structure, which consists of 20 municipalities. Decisions come from the top to the bottom and the feedback goes in the opposite direction (see Figure 4.2). The Tripoli municipality is the most important one in the mezzo level for the following reasons:

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<sup>12</sup> During the 1970s Qaddafi’s political economic theorising took on a concrete form through the publication of the third universal theory in the Green Book. The latter explains all the theory’s implications.

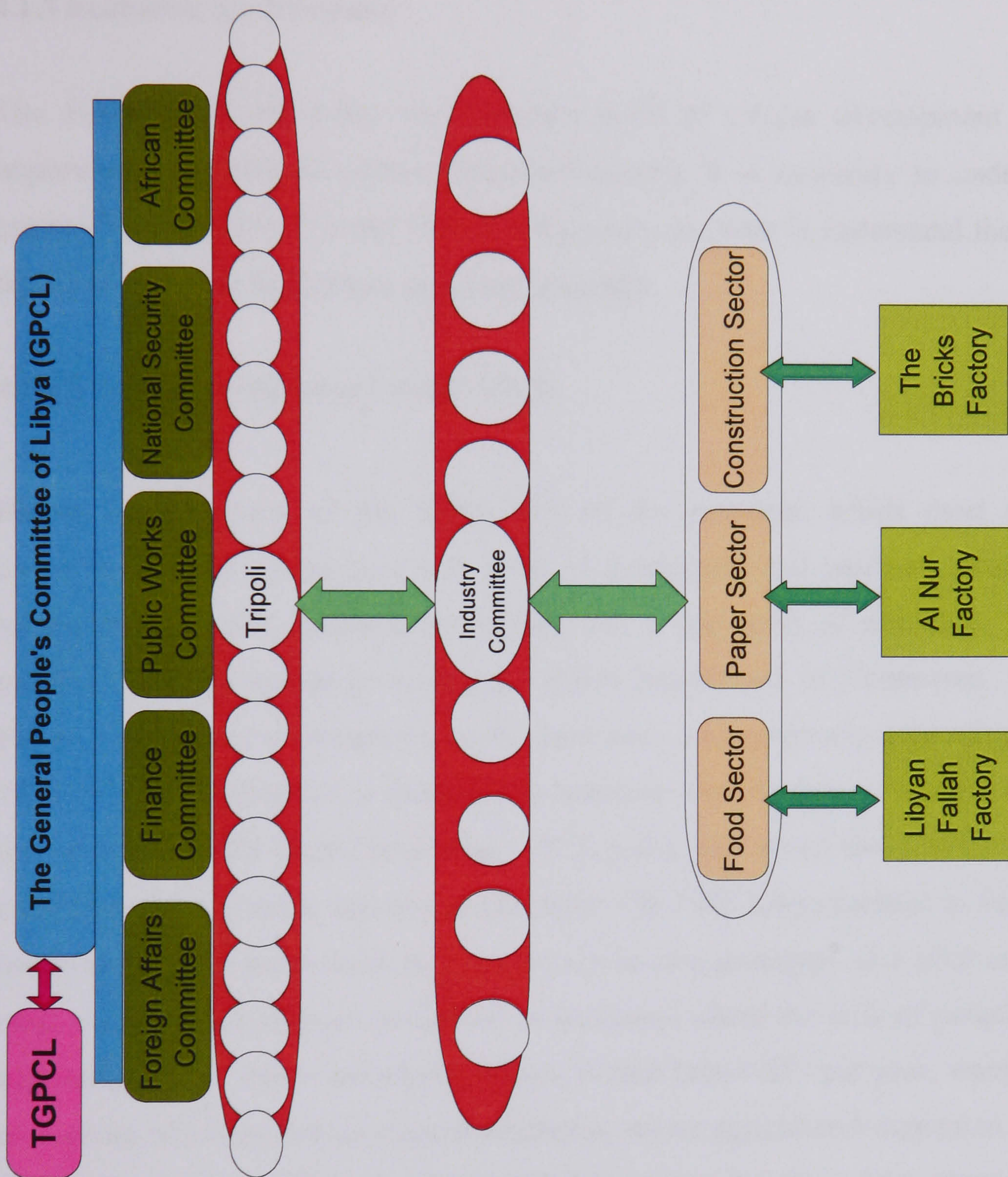


- Tripoli is the capital city of the country.
- Most of the public facilities are established in the Tripoli region.
- Most of the development research centres are located in Tripoli.
- Tripoli's important location on the coast of the Mediterranean Sea.
- The main airport and seaport are in Tripoli, therefore it is regarded as the main gate of transportation between Africa and Europe (see section 4.3).

It can be seen from Figure 4.2 that each municipality has a complex structure of ministries, locally called committees. Taking the Tripoli municipality as an example, the research region consists of nine committees (ministries); the Transportation Committee; the Security Committee; the Finance Committee; the Health Committee; the Industry Committee; the Education Committee; the Agriculture Committee; the Public Works Committee and the Economy Committee. Each of the nine committees has a direct connection with the Tripoli municipality system. The Industry Committee (ministry) of the Tripoli municipality is the most important part of the structure chain because it consists of the Food, Paper and Construction Materials sectors (which are the focus of this research).

As a result of the importance this sector, the decision-makers paid more attention to the development of the case study industries to accomplish greater self-sufficiency in local products and reduce the dominance of the public sector. Consequently, many public factories have had their ownership transferred to their employees (see Chapter 5). Understanding the influence of the political factors in the Libyan context on managing and controlling the day-to-day affairs in the Libyan private sector is one of the objectives of this research. According to the research interest, the Libyan Fallah Factory from the Food product sector; the Al Nur Factory from the Paper product sector and the Bricks Factory from the Construction Materials sector have been chosen as case studies for such research, in order to gain an in-depth understanding of the MCSs in these industries within their developmental environment (see Figure 4.2 and Chapters 1, 6, 7 and 8).





**TGPCL:** The General People's Congress of Libya

**Figure 4.2: The Libyan Political Structure**



### **4.1.3 Economic environment**

The discovery of oil marks the departure point of Libyan development plans and improvement of non-oil sectors (industrial sector). It is necessary to understand the country's situation before and after this discovery in order to understand the impact of the oil revenues on the Libyan development plans.

#### **4.1.3.1 Before the discovery of oil (1959)**

Before the discovery of oil, Libya had all the problems which most developing countries struggle to solve; a low level of production and national consumption; a serious trade deficit, balanced by foreign aid, a low level of education, health and unsuitable natural resources investment (USA Department of Commerce, 1970, p.5). Facets of economic development at the time were also extremely depressing (Higgins, 1959). Benjamin Higgins, a specialist in economy who worked as advisor to Libya in the period of 1950s (Bait-Elmal *et al.*, 1973, p.84), said about the country's economic condition and economic features at that time: "In 1952 Libya seemed to be an almost hopeless case. Its great merit as a case study is as a prototype of a poor country. We need not construct abstract models of an economy where the bulk of people live on a subsistence level, where per capita income is well below \$50 per year, where there are no sources of power and no mineral resources, where agricultural expansion is severely limited by climate conditions, where capital formation is zero or less, where there is no skilled labour supply and no indigenous entrepreneurship. When Libya became an independent nation ... it fulfilled all these conditions" (Higgins, 1968, p.819). Libya after its independence remained under poor conditions, especially in terms of its national economy, because there was extreme underdevelopment (Farly, 1971, p.106). The level of resources for development was very low (only a few types of industries and agriculture) and before the discovery of oil the Libyan economy was very weak and unable to cover the expenses of the regions and the federal government. There was also a deficit in the balance of trade and payment (Higgins, 1968, p.820). Before the



discovery of oil, the Libyan economy was thus faced with the same problems all developing countries face. Hence, the Libyan economy needed a big boost to free it from these poor conditions.

#### **4.1.3.2 After the discovery of oil**

Oil was discovered in Libya in 1958, and production and exportation in commercial quantities began in 1961. As a result of this discovery the Libyan economy underwent rapid growth, described by one economist as follows: “If the economic growth occurring today in Libya were described without identifying the country, it would be dismissed most likely as an extremely hypothetical case, too dramatic to be real” (Ragaei El- mallakh, The middle East Journal, 1969, p.308).

Oil income played an important role in the development of Libyan society and there is no comparison between the Libya of today and Libya before the discovery of oil. Richard H. Sanger (1975) described the transformation thus:

“The cities had become construction camps with noisy bulldozers levelling buildings and cement trucks pushing through the traffic jams with loads for the every-hungry building cranes which dominated the sky line. In and around the chief cities and towns rose block after block of new housing ... Hospitals of standard design were being built in half-dozen lots ... The giant campuses of the universities of Tripoli and Benghazi were the most impressive in Africa ... Above many side streets and garden suburbs the tall chimneys of new factories rose behind the minarets, their dark smoke clouds proof of the boom in cement, reinforcing wire, plumbing fixtures, textiles, food processing, and most successful of all, the drive to expand electricity” (Richard, H. Sanger, 1975, pp.413-414).

Oil income became the most important source of capital formation, so Libya did not have to face the problem of capital formation, a problem afflicting the economies of most developing countries. However, it is undeniable that there are some problems that the Libyan economy faced: inflation, a scarcity of trained decision-makers or skilled labour, dependence on the oil sector as a single source for economic performance, and the low rate of private capital formation are some of the most critical problems.



The Libyan government has recognised that oil resources will run out in the near future. Consequently, most of the oil revenue is now directed to improving non-oil sectors, especially industrial sectors. The main target of all development plans has been to achieve a greater self-sufficiency in goods by using local sources of raw materials. Food, Paper and Construction Materials industries have gained the trust of policy-makers as playing a vital role in accomplishing development targets. The importance of the case study sectors in the Libyan economy encouraged this researcher to choose them as case studies to attempt to understand the implementation of MCSs in these sectors within their environmental developmental context.

#### **4.1.3.3 The 1990s**

During the period 1990-1993 the development expenditures budget was estimated at about US\$ 2 billion, two times less than the previous budget of 1989-1992. This reduction of the development budget was the result of the decline in international oil prices. From the late 1970s up until 1991 the government controlled both the production and service sectors. However, crises in the economy prompted the government to introduce a series of economic liberalisation measures at the beginning of 1988; for example, many private activities were established; in September 1988 the government proposed an expansion in the privatisation programme and announced that Libya would be able to import and export without limit (Fisher, 1990). This restructuring policy was initiated and regulated through the issue of Government Act number (9), dated 5/9/1992. The main objective of this Act was to regulate and enhance the role of private sector activities in the national economy. The African Development Report (1994) included various important points such as:

- The economic area open for private and individual initiatives will include production, distribution and services. These activities will take place in areas such as agriculture, industry, commerce, tourism, transport, and finance, as well as in the private practice of professionals. The implementation of these private activities can be achieved through various channels, such as joint companies, corporation and public companies, family and individual activities.



- Based on a recommendation of the General People's Committee, public or joint enterprises could be sold to private ownership. According to this recommendation, the Industrial Committee has transferred 146 public factories to private ownership. For the scope of this research, Food, Paper and Construction Materials factories will be discussed in more detail (see Chapters 5, 6, 7 and 8). Gaining an in-depth understanding of the impact of those Libyan economic factors, which have influenced the MCSs in private sector organisation, is essential in order to gain a better and more holistic understanding of the phenomenon under investigation.

The most important international economic action against Libya was in 1992, when the UN issued its resolution No. 748 to impose economic sanctions on Libya. Since the mandatory sanctions under Security Council resolutions 748 (1992) and 883 (1993) were first imposed, the industry and mining sector has continued to suffer considerable losses and other material damage. The total financial loss resulting from these increasingly adverse effects on all aspects of industrial development amounts to approximately US\$ 4,150,677,942 (The Libyan Mission Report, 1996). Increasing the sanctions and bans on the Libyan economy would obviously hurt the Libyans, but it would also hurt Tunisia, Egypt, Chad, Niger and other neighbouring countries whose nationals work in Libya. As a response to these sanctions Libya had signed a number of economic agreements with these countries. According to these agreements, the countries were allowed to export their local products to the Libyan market without taxes and customs. To understand the impact of these sanctions and agreements on the MCSs in the Libyan private organisations see Chapter 9.

#### **4.1.4 The regulatory environment in respect of business activity**

Economic and business affairs are controlled by laws, which are usually enacted by the government and related to the change of future needs in the society. Today, the role of the government has increased considerably, as Dr. Scott forecast more than fifty years ago. The rapid consolidation of industry and capital into monopolistic positions of power tended to destroy the idea of laissez-faire and the beneficial effects of the free



enterprise system. Dr. Scott (1970) explains as follows: “It is a patent fact that important economic groups do not now have faith in market control. Indeed, those who belong in one or another group of the faithless constitute a large majority of the population they look to other agencies, for protection of their economic interests rather than to their own efforts in a competitive market.” Governments have always been involved in the economic aspects of societies to try to maintain full employment and provide security for the people. Libya is no exception and several laws have been enacted, some of which have been replaced and modified to adapt to the changes in the social life and economy. Food, Paper and Construction Materials industries were affected by many state laws and regulations. A brief explanation of the important laws, which have had a direct influence on the MCSs in the case studies industries of this research will be the subject of the next subsections.

#### **4.1.4.1 The Libyan commercial code**

In November 1953 the Libyan commercial code (LCC) was introduced and has been amended many times to satisfy the changing needs of Libyan society. This code consists of various books and requires that from each Food, Paper and Construction Materials company an enterprise must have at least the following books: a) a journal, and b) an inventory and balance book (Libyan government, 1972, article 58). Before using the books to record the process of the activities the court should stamp them with serial numbers consecutively.

According to the requirements of the LCC, every Libyan factory should prepare a yearly balance sheet and profit and loss account and the financial statements must be reported to the general assembly of shareholders for approval (Libyan government, 1972, article 572). A copy of all the approved statements must be submitted to the commercial register in the factories’ region within thirty days of the date of approval and this copy is to be agreed by the directors’ report and auditing board reports (Libyan government, 1972, article 583). In addition to the Libyan commercial code, law No.65 of 1970 was passed on May 2<sup>nd</sup>, 1970 and published in the ‘Official Gazette’ in June 1970 (Meredith and Ibrahim, 1972, pp.209-217). The aim of this law was to determine certain



provisions concerning Food, Paper and Construction Materials factories and their supervision. Some of the important provisions include that:

1. each person who exercises the trade profession should be of Libyan nationality;
2. the percentage of the capital owned by Libyans in the commercial companies must not be less than 51% of the total capital;
3. the directors in all the companies must be Libyan;
4. the number of Libyan workers in any company should be at least 90% of the total number of the workers.

#### **4.1.4.2 The income tax law**

The income tax law was introduced for the first time in Libya by the Italian government in 1923. As the central Bank of Libya wrote in one of its economic bulletins: “Libya witnessed this type of financial obligation for the first time in its history in 1923. The Italian government introduced this tax applied in Italy during that period first in Tripolitania by the provincial decree No.501- collection (a) Issued on the 26<sup>th</sup> May, 1923, after Tripolitania has been divided into three regions for tax purposes...” (Central Bank of Libya, economic bulletin Sep-Dec, 1971, p.154). The first Libyan income tax law was issued in 1968. The present income tax law, No. 64, enacted on September 19<sup>th</sup> 1973, negated the old law No.21 of 1968. In the present income tax law there is a classification of many types of incomes and specific rates are levied on different types of incomes such as: incomes from agriculture, commerce, industry, real estate, wages and salaries, persons abroad, residents in the country, free professions, deposit and saving accounts in banks. Taxes are different according to the income tax law on all these incomes.

Some companies have adopted the tax law for external financial reporting (Bait-Elmal, 1973, p.95). For example:

1. The method, which the company selects to calculate the depreciation should be based on the straight-line method and on the historical cost of the asset.



2. All costs paid by the company until the commencement of its operations may be consumed against the total income over three to five years using the straight-line method (Libyan government, 1973, articles 55 and 56). This feature of law follows the French law, which allows for the possibility of deduction of capital expenses from revenues (Kilani, 1988, p.130).
3. Donations to charities are limited to not more than 2% of the taxpayer's net income (Libyan government, 1973, article 55).
4. When the result of the account for the year is closed with a loss, this loss can be carried forward for five years (Libyan government, 1973, article 59).

## **4.2 Development within a Libyan context**

Development is a word that has two different connotations. One connotation is related to the processes of a biological organism and denotes how nations or societies somehow and somewhere begin, then grow or develop. The second is that development often means simply 'more'. The social interpretation of good and bad times in terms of more is that "good times are those moments in which we think we have more than previously and bad times are those in which we think we have less" (Sklair, 1994, p.5). Thus, the demand for development is about two main issues; on the one hand, development is supposed to mean greater internal equality, that is, fundamental social (or socialist) transformation. On the other hand, development is supposed to mean economic growth, which involves 'catching up' with the leader. The indicator of development in the world is the number of countries that have successively developed or industrialised during the period 1750-1950 (Sklair, 1994, pp.10-14). Development from the Libyan decision-makers' perspective is a process of accomplishing greater self-sufficiency in goods and services to meet the national demand and to become more independent of imported products.

Furthermore, the main target of development plans is to support the non-oil sector, so the industrial sector is not dependent on a single sector (oil) only (see section 4.2.4). The industrial sector in general and, Food, Paper and Construction sectors in particular are paid more attention by the state with the aim of their playing an essential role in



Libyan economic development (see Chapter 5). Yet most Libyan people seem to have little understanding of the state objectives for development. Identifying the reasons for this misunderstanding and the contradictions (if any) among the state development objectives and people's objectives in these case study industries is one of the aims of this study. Libya, as a developing country, has had various development plans, especially since the discovery of oil. For the purpose of this research, the Libyan Food, Paper and Construction Materials industries environment is discussed in more detail below.

#### **4.2.1 The development plans of Libya since independence**

Many definitions of development planning have been found in the literature. Enthoven (1973) defined development planning as “the preparatory evaluation and decision-making process of a forward-looking character for an economy, in which alternatives have to be outlined measured, weighed, and priorities for the use of resources established”. Todaro (1985, p.464) described economic development planning as “a deliberate governmental attempt to co-ordinate economic decision-making over the long run to influence, direct, and in some cases even control the level and growth of a nation's principal economic variables (income, imports, etc.) in order to achieve a predetermined set of development objectives.”

Development planning was initiated in most developing countries as a result of the failure of the market to determine the prices of production factors in the third world. The UN (1965) described the situation thus:

“The need for using appropriate criteria for selecting projects arose because of the failure of the market mechanism to provide a proper guideline. In less-developed countries, market prices of such factors of production as labour, capital and foreign exchange deviated substantially from their social opportunity costs and were not, therefore, a correct measure of the relative scarcity or abundance of the factor in question” (The UN, 1965, p.12).

The realisation that oil would not be an unlimited resource in Libya motivated decision-makers to formulate economic development plans. The first of these ran from 1963 to 1968 after the government established the national planning council to consider all the



policies for planning and development. Development plans in the 1960s aimed to improve the quality of people's lives and increase investment in the public services. The objectives of these plans are summed up by Rawle Farly (1971, pp.198-200) as follows:

1. To ensure the early improvement of the standards of living of the people, particularly those who have a limited income, because about 80% of native Libyan citizens were engaged in agriculture and animal husbandry. They live away from the capital city with a lack of education, health, communications, or financial resources. Hence, these native people do not benefit from any economic prosperity.
2. To give special consideration to the agricultural sector, being the source of supply of most of the essential consumer goods, besides being the source of income and employment for the majority of the Libyans; to be attentive to industry; to improve the productive efficiency of farmers and labourers and to encourage the private sector to invest in these fields.
3. To permit the public sector to continue investing in such services as education, health, communication and housing, together with other sectors, as a requirement to consolidate the basic elements for rapid economic growth.
4. To organise import policies so as to avoid the importation of goods which can be produced in the country to ensure protection of the national products from the danger of inflation and also ensure provision of sufficient supplies of capital goods needed for development. To further strive to step up local production and to adopt an appropriate customs policy for its protection and in this way gradually and continuously substitute local production for the mass of such imports.
5. To take such monetary, financial and commercial measures ... all in a co-ordinated effort ... as may be necessary to ensure increased revenue and to enforce a strict control on expenditures.
6. To take steps to meet a lack of information and statistical data necessary for planning, by strengthening existing statistical data and by studies and research work.



Table 4.1: Development Budget, 1963–1992, Actual and Planned Expenditures in millions of Libyan Dinars.

Source	1963-1968		1970-1980		1981-1990		1970-1992		
	value	%	Value	%	Value	%	Value	%	% AP
Agriculture	65	12	2,393	21	2,152	14	5,190	18	87
Industry	29	5	1,655	15	2,902	19	4,732	17	84
Electricity	56	10	1,346	12	1,396	9	2,817	10	85
Transportation	92	17	1,430	13	2,330	15	3,958	14	95
Housing			1,374	12	1,599	11	3,154	11	87
Public finance			1,000	9	2,024	13	3,231	11	97
Education service	48	9	711	6	977	6	1831	6	72
Health service	16	3	328	3	556	4	989	4	67
Other services	82	15	471	4	880	6	1,522	5	67
Total non-oil sectors (1)	551	100	1,0707	95	14,815	98	27,422	97	86
Oil and gas sectors (2)			546	5	370	2	1,002	4	67
Total Actual Development Expenditure (1+2)	551	100	11,253	100	15,184	100	28,423	100	
Planned Development Expenditures	169	100	12,368	100	18,355	100	33,518	100	
% of Actual Expenditure to Planned Expenditures		326		91		83			85

**Note:** %AP= percentage of Actual Development Expenditures to planned Expenditures; for the period 1963-1968: value = 162.2 and % =29.4  
**Sources:** for 1963-1968: Libyan Ministry of planning, 1980a, p.13; for 1970-1980 and 1980-1990, Libyan Secretariat of Economics and Planning, 1991, pp.1-9; and for 1970-1992 Figures: Libyan Secretariat of Planning, Trade and Finance, 1993, p.8.

With the coming of the revolution in 1969 the Libyan government adopted a socio-economic policy with objectives mainly directed at:

1. increasing investment in the non-oil sector;
2. reducing the dependence on the oil sector as the primary source of income;
3. controlling underlying development of economy and society;



4. Identifying the important activities and the amount of investment for the developing programmes according to the amount of crude oil the country will produce (Ministry of Industry, 2000).

After the Libyan revolution the economy underwent some very significant changes in policies, especially in an increase of the percentage of non-oil sectors in the budget of the country and decrease of the contribution of the oil sector (see Table 4.1).

Investment in the 1980s concentrated on the industrial sector (after the failure of the agricultural sector) to become the first sector to produce revenues high enough to cover all the country's needs without relying solely on the oil incomes. Investment was instead channelled to the industrial sector, with an emphasis on Food, Paper and Construction Materials industries with the aim of achieving greater self-sufficiency in their products. The overall percentage of industrial development rose from 14.7% during the 1970s to 19.1% during the 1980s. In contrast, agricultural development declined from 21.3% in the 1970s to 14.2% in the 1980s (Table 4.1). The general economic objectives of the development plan are summarised by the Libyan Ministry of Planning in one of its reports as follows:

1. Increasing total production in all sectors in such a way so as to attain an overall compound growth rate of the real Gross Domestic Product of 10.7% per annum. This will be primarily reliant on the non-oil sectors which are planned to grow at a rate of 14.1% per annum while the growth rate of the activity of the extraction of crude oil and natural gas will be kept at 7.8% per annum.
2. Since the objective of planning in the final analysis of the development was the improvement in the quality of life for the Libyan citizens, and hence their welfare and well-being, the plan aims at the growth of individual consumption both of directly purchased goods and services and of those services provided free by the state (education and health). Therefore, private final consumption is planned to grow at a compound rate of 9.4% per annum, while the growth of public final consumption will be 9.6% per annum.



The industrial sector has played a significant role in the Libyan economy. However, one problem has been that local demand for skilled labour far exceeded supply and all the technicians' skills had to be improved. Also, the limited local market made the investments in the industrial sector less than in the other sectors. In addition, raw materials and other industrial base requirements were very limited. Farley (1971) explained the limitations as follows:

“The Libyan market was clearly small; power and fuel resources were limited; raw materials were confined to a few limited and irregularly supplied agriculture resources except for significant deposits of natural salt; transportation facilities were largely non-existent for the country as a whole; and local management, capital, entrepreneurship, and industrial skills remained largely invisible except for some development in Cyrenaica” (Farley, 1971, p.139).

As a result of these limitations, industrial activities were very limited and depended on agricultural resources. Therefore, the industrial activities included mainly fish processing, flour milling, olive oil production, food products, tobacco, shoes, printing and building materials. The majority of these manufacturing activities were located in the big coastal cities of Tripoli and Benghazi.

As an effect of the discovery and refining of oil in Libya in 1961 the industrial sector has grown significantly and the industrialization of the Libyan economy is now a high priority item on Libya's economic development agenda. The government has consequently initiated a number of steps to encourage the establishment of private industries, for example, the establishment of the industrial Bank of Libya to provide businessmen with loans to start their business, and the establishment of the industrial research centre to help with implementing the development plans by providing technical and economic advice regarding the activities. Food, Paper and Construction Materials factories were established in the main cities (Tripoli and Benghazi) to try to accomplish the development target of meeting local demand by a greater self-sufficiency in products.

From the Libyan Secretariat of Economic and Planning report (1991) it can be concluded that a huge development in investment in the period 1970-1991 was related



to the increase of international oil prices and the policies of the government to reduce dependence on the oil sector. As a result, the structure of Libyan investment changed to the benefit of the non-oil sectors, yet despite large investment in these sectors (resulting in a high percentage of production from non-oil sectors), the dependence on the oil sector is still heavy. The country faced many problems during the implementation of the development plans and these problems have hindered the achievement of the objectives of the development plans. Farley (1971) described the planning problems as follows:

“Popular expectations of planning were aroused, but not popular understanding or popular participation. Planning institutionalisation was there, but not the minimum number of planning administrators, technicians, and expertise ... Oil resources were there, but quantified data determine financial and other strategy were absent ... Planning co-operation between ministers was weak, project execution frequently costly; project maintenance negligent in many areas; planning follow-up weak ...” (Farley, 1971, p.229).

Libya has continued to have such problems because it still needs to implement effective socio-economic development plans. Hence, understanding the relationship between the external environmental factors (social, economic and political) and the organisational processes (MCSs in Food, paper and Construction Materials industries) is critical in order to achieve the objectives of this research.

### **4.3 Selection of the Tripoli municipality as the site of this research study**

Tripoli was chosen as the site of this research for its history and importance. Tripoli is an ancient city, one of the four main Phoenician cities in North Africa (the other three are Karthag, Sabrata and Liptes). In 24 BC it was invaded by the Garamants who came from the South of Libya. At the beginning of the third century it was given the name ‘Tripolitanos’, meaning ‘the three cities’, i.e. Sabrata, Ouia and Liptes. The Arabic name of Tripoltanos is Tarablus and it received this name after the Arabs conquered it in 22 Hijri (643 AD). Some historians gave Tripoli the name ‘The White City’ because of its white painted buildings. Much later, in July 1535 the Spanish invaded the city, but their reign was short-lived, and in August 1551 the Turks defeated the Spanish and the



Ottoman rule of the region began. The Turks named Tripoli ‘Tarablus al Gharb’ or ‘Tripoli-West’ since they already had another Tripoli in Lebanon.

In 1958 the commercial exploitation of oil began and the rate of growth of Libya’s economy went at an unprecedented rate. This growth led to industrialisation and rapid urbanisation, accompanied by the social transformation that has changed the socio-economic and physical structure of the country much more deeply and at a more rapid pace than had been estimated by planners. The physical plans prepared in the period 1966/1969 did not anticipate the recent rapid rate of urbanisation and as a result, most of the towns and cities have experienced an accelerated growth rate and development, which in many cases has exceeded the boundaries of the obligatory plans. In particular, Tripoli city began to dominate the country’s political and economic life. Within this city, the phenomenon of over-urbanisation has occurred emphasising regional differences. This has had negative effects on the country as a whole and has put a great strain on the existing services, infrastructure and resources. The positive effect of the recent rapid rate of urbanisation in the Tripoli region has been the improvement of the level of services and industries (these case studies) to meet the local demand for food, paper and buildings. Consequently, Food, Paper and Construction Materials industries have received the great portion of the allocation of the state budget.

#### **4.3.1 Location**

Tripoli is the capital city of Libya and is located in the north-western part of the country, on the Mediterranean coast. The total area of Tripoli is 225,200 square km over an area that represents around 13% of the total area of the country. Tripoli City is considered to be the most important urban area in the whole country because it is the capital city and has the greatest concentration of national services and facilities.

#### **4.3.2 Population of Tripoli municipality**

Tripoli city has the largest concentration of the population and socio-economic activities in the country. Within a 40-year period from 1954 to 1994 (census 1994), the



population of the region increased nearly four times and doubled in the country as a whole (as shown in Table 4.2).

Table 4.2 Comparative data: Libya, Tripoli municipality, in the year 1994.

Index (unit)	Libya	Tripoli Municipality
Area (km²)	1,785,500	225,200
Population	4,640,000	3,018,000
Population density (person/km²)	2.6	13.4
Employment	1,219,500	725,500

Table 4.3 Population growth from 1954 to 2000.

	Years					
	1954	1964	1974	1984	1994	2000
Tripoli Municipality	730,000	1,006,000	1,428,000	2,018,000	3,018,000	3,621,600
Libya	1,089,000	1,565,000	2,349,000	3,250,000	4,640,000	5,104,000

From Table 4.3 it can be seen that population growth in the Tripoli region has accelerated, in particular since 1970, when the annual rate of population growth exceeded 7.0%. This dynamic population growth over sixteen years was not only a result of a high natural increase, but also a consequence of migration from rural to urban areas. Thus, since 1974, the total population in the Tripoli region has increased by about two million inhabitants.

#### 4.4 Summary

From an examination of all development plans since 1969, it is clear that the Libyan economy is still dependent on the oil sector. Consequently, oil exportation is of great importance to achieve the development policy objectives. Strong attention has been paid to moving away from this dependency on the oil sector by improving non-oil sectors such as Food, Paper and Construction Materials industries so as to achieve greater self-sufficiency in basic products. Although the homogeneous Islamic heritage united the



country, this heritage was less attached specifically to Libya (with its territorial boundaries) so much as being a basis on which a nation could be built. Instead, the essential component in the Libyan environment, which provides an infallible source of cohesion and underpins its cultural identity is the Islamic religion. Islam, provides both internal cohesion and at the same time a comprehensive framework for the external relationships that link cities to the surrounding areas.

This chapter has focused on the economic, social, and political aspects of Libyan society within the Food, Paper and Construction Materials industries context, which is the macro context of this research, in order to gain an in-depth understanding of role of MCSs in these industries within their environmental developmental context. The next chapter focuses on the Libyan industrial sector.



## **Chapter 5: The Libyan Industrial Sector with a Focus upon Particular Industries**

### **5.0 Introduction**

The previous chapter dealt with the socio-economic and political context of the research sites. The objective of this chapter is to elaborate on the context, more specifically on the Libyan industrial private sector (Food, Paper and Construction Materials industries) so as to enhance understanding of MCSs in the developmental environment focused upon. To accomplish this aim, this chapter is divided into a number of sections: a discussion of industrialisation in Libya; an outline of the relevant Libyan industrial context focused upon – thus a detailed exploration of this context and its development plan (2001-2005) is provided for the study; a highlight of the Libyan public sector; a detailed description of the private sector and privatisation in general; a summary.

### **5.1 Industrialisation and Libya**

To understand the Libyan industrialisation process, it is worth highlighting the history of this process. The takeoff of industrialisation in developing countries in general and in Libya in particular has its roots in interaction with the western world and, in particular, with the UK. An understanding of the Libyan industrialisation process is important for this research, because the Libyan industrial sector provides the setting for the research site.

Industrialisation in developing countries, especially the Arab nations, began in the second half of the 20<sup>th</sup> century, just after the discovery of oil in their deserts. Arab countries are the world's largest oil producers and have the world's largest pool of proven crude reserves. They also have large reserves of natural gas. Moving 'downstream' to integrate the various phases and sequences of production, processing, shipping and marketing is a very efficient way to encourage industrialization. However, the important fact about oil, which must be considered by the Arab nations, is that the



end of the oil era is in sight, and, because most of the Arab nations need long-term projects and plans, the gestation period of development of the regions could extend beyond the life span of the hydrocarbon resources of the regions. Libya, as an Arab country, must seriously consider developing an alternative sector to the oil sector. The Libyan industrial sector, with its particular activities (Food, Paper and Construction Materials industries) is regarded as a candidate sector to play a vital role in the economic development plans, and will be the subject of the following sections.

## **5.2 The Libyan industrial context**

Libya enjoys a distinguished geographical position overlooking the Mediterranean Sea and a point of connection between the African and European Continents (see Chapter 4). It is thus considered the main seaport of Africa. Moreover, it enjoys a favourable investment climate with many attractive features, including raw materials in abundance locally, energy resources and commercial seaports and airports. Since 1969, a number of considerations have arisen that led the Libyan policy makers to give serious thought to the desirability of placing a greater emphasis on the industrial sector in general and the Food, Paper and Construction Materials industries in particular. The likelihood that the oil sector will not continue to propel economic growth to the extent that it has done from the 1970s, (because of both the low world price and diminishing exportable volumes), poses the need for an alternative engine of growth, and the non-oil industrial sectors are the most likely candidates for this mission.

In the 1970s, the revolutionary government paid more attention to the development of the public industrial sector:

“The industrial sector is of special importance in the development strategy in the Jamahiriya. This is because of the critical role it has to play in the process of transformation and restructuring of the economy and hence the progressive decrease of the degree of dependency on the oil sector” (Ministry of Industry, 2000; The second development plan 81-86).

The policy elaborates with the point that the first priority “in industrial development is given to the basic needs of food, shelter and clothing” (Ibid, p.22). The second priority



is on the development of the construction materials and oil refining industries. The third priority is on the development of the other industries such as paper, iron, steel and glassware activities. For the purposes of this research, the first, second and third state priorities (Food, Paper and Construction Materials industries) were chosen as case studies to examine and understand the relationship between socio-economic and political factors and organisational processes (MCSs). In 1970, the National Public Organisation for Industrialisation was established to implement the development plans of the industrial public sector. In addition, the allocation of money for this sector in the investment budget increased after the early years of the revolution. In the development plan from 1973 to 1975 nearly 13% of the plan's investment was allocated to the industrial sector. Around 329 million LD were allocated to fund 74 industrial projects in order to increase industrial production and its contribution to the national income (Libyan Arab Republic, 1973, pp.205-207).

The Libyan policy decision-makers prioritised the present case study industries. Moreover, they placed special emphasis on ensuring sustainable economic growth and providing substitute sources for revenue in order to build a balanced economic structure and achieve a varied productive economy. Objectives 1 and 2 of the industrial development plan of 2001-2005 supported the goals of liberating Libyan society from dependence on rent from oil from foreign demand and the strengthening of a diversified and intermediate production by:

1. Pursuing the policy of imports replacement to achieve greater partial or complete self-sufficiency in clothes and building materials to meet the needs of citizens.
2. Benefiting from natural local resources such as building materials, silica, and agricultural products.

Manufacturing was a development challenge that was to be unquestionably accepted and tackled in order to find substitute resources for oil as a source of public revenue. The development policies and plans (1990-1995; 1996-2000; 2001-2005) reflect the importance of the research case study industries (see Tables 5.1 and 5.2). The development process in Libya is seen as follows:



Table 5.2: Development Bank Loans (Million LD)

- considering social and developmental effects;
- planning spatial development and building in remote areas;
- creating a pool of technical and administrative staff;
- ending monopolies of technical means by foreign companies (most oil companies are foreign companies and they used their own personnel and equipment);
- lifting the dependence imposed by these monopolies.

Table 5.1 Saving and Real Estate Investment Bank Loans (Million LD).

Year	Disbursement of loans for housing and construction projects		Total
	Housing loans (million LD)	Construction projects (million LD)	
1990	26.4	3.3	29.7
1991	30.0	2.5	32.5
1992	8.6	1.3	9.9
1993	12.4	1.3	13.7
1994	19.0	1.4	20.4
1995	18.0	1.8	19.8
1996	18.6	2.4	21.0
1997	31.6	4.7	36.3
1998	17.2	20.2	37.4
1999	9.9	25.4	35.3
2000	37.7	17.0	54.7
2001	75.5	18.7	94.2
2002	302.9	8.8	311.7

Source: Saving and Real Estate Investment Bank, Tripoli, 2003.



Table 5.2: Development Bank Loans by industry (Thousand LD).

Year	Food industries (Thousand LD)	Construction materials (Thousand LD)	Paper industries (Thousand LD)
1999	269,4	304,7	50
2000	41,507	24,455	8,144
2001	47,948	20,533	7,305
2002	73,686	51,138	2,701

Source: Development Bank, Tripoli, 2003.

In 1969 one of the basic characteristics of the Libyan economy was that it was largely supported by a single resource: it depended mainly on the exportation of crude oil. In addition, it was distinguished by the limited performance and scarcity of other productive bases. The oil sector contributed a high proportion of the Gross Domestic Product (GDP) and the contributions of other sectors were limited. Industry was reliant on a few factories that were owned and managed by the public and private sectors. Imperfections in the Libyan economic structure were the main inducement for the adoption of industrialisation as a correctional method and also to add more balance to the national income resource. Economic studies indicate that the Food, Paper and Construction Materials industries are the most important industries in this respect and can play a major role in achieving social, economic and political development. National economic capacity grows by fulfilling the increase in demand for the products of these industries. Their importance motivated this researcher to attempt to understand the MCSs in their developmental environment.

**5.2.1 The basic objectives of the industrial development strategy prior to 2001**

Because of the importance of Food, Paper and Construction Materials industries in social and economic development, these industries have been given special attention by the decision-makers. Planners had to set some perspectives related to industrial development strategy to be implemented through the social and economic development plans, which included the three-year plan of 1973-1975 and the development plans of



1976-1980 and 1981-1985. The basic objectives of the industrial development strategy were as follows:

- Creating work opportunities (for both men and women) in different industrial sectors and working towards national experience and skilled technicians.
- Diversifying the economic structure through increasing the importance of the contribution to the GDP of the Libyan case study industries.
- Diversifying the export structure through the participation of Food, Paper and Construction Materials industries in the national development exports.
- Promoting economic efficiency among the existing Food, Paper and Construction Materials factories by examining the problems that would hinder the achievement of the goals and therefore implementing a precise reform of the industrial sector situation.

### **5.2.2 Major problems of and obstacles facing the industrial development strategy**

During the period of 1969-1996, the industrial sector faced several problems affecting its production units (including of the Food, Paper and Construction materials industries) and its capability of achieving the development goals. Fadal and Kamoshy (1995) summed up the problems as follows:

1. A decline of industrial sector investment since 1980, preventing the emergence of new industrial projects and the development of existing ones.
2. A shortage of skilled personnel who would be able to carry out, for instance, periodic, accidental and programmed maintenance for the equipment and production lines.
3. A poor infrastructure for most existing establishments making it necessary for these establishments to provide secondary and basic utilities themselves, thus burdening the sector with expenditure on unproductive assets.
4. One of the aims of industrial development was to produce goods to replace imported goods. Therefore, many factories were established for this purpose, for instance the Construction Materials industries, which are using 100% local raw



materials. Yet many other industries are dependent on imported raw materials and they have thus inadvertently increased the burden of foreign currency payments.

Understanding the state development objectives in the industrial sector in general and in the Food, Paper and Construction Materials industries in particular is of great importance for this research. Moreover, understanding the development objectives at a macro-level enables the researcher to identify any contradictions between the state's objectives and those of employees at a micro-level (in the case factories of the case studies). This understanding of state development objectives is attempted in order to achieve a better understanding of MCSs in Libyan private factories within their environmental and organisational context.

### **5.2.3 The industrial development plan of 2001-2005**

The general objectives of the development plan consist of reform of the national economy establishing a strong base to achieve a permanent development and reap the advantages of the previous development plans. The common aims of the development plan rest on the following:

1. achieving economic diversity through the establishment of permanent development resources in addition to the oil sector;
2. activation and development of the productive and service sectors and increasing benefits from their resources to achieve economic diversity;
3. activation and development of production factors, work and capital in particular;
4. achieving growth in GDP in excess of the growth of the population in order to achieve an improvement in living standards;
5. conservation of natural resources and working towards the best investment of such resources;
6. adoption of a policy of diversifying foreign currency resources, and encouraging exporting industries;



7. giving the private sector the opportunity to play an important role in exploiting resources and re-activating the industrial sector by the establishment of the private sector;
8. restructuring the public sector by launching the privatisation process and transferring the public ownership to private sector;
9. reviewing and simplifying laws and regulations related to economic activities in both public sector and private sector;
10. encouraging the participation of foreign capital in the development process through the implementation of the investment Law No.5 dated 1997.

#### **5.2.4 The strategies and the general policies of the industrial sector for 2001-2005**

- **The strategy**

As a result of the key role that the industrial sector plays in initiating achieving and pacing the economic development, its productive capability is higher than that of the other sectors, and its development is therefore considered as one of the fundamental goals for the achievement of permanent economic development. Furthermore, the industrial sector contributes to technical advancement and education, both of which are considered basic conditions for economic development. Industrial sector improvement has thus received top priority in development plans and budgets. Over three successive decades (the 1970s, 1980s and 1990s), the development strategy has aimed in its first plan towards improving specific industrial activities, which depend on local raw materials. In line with the balanced growth needed to achieve greater self-sufficiency of necessary goods and products, this has been extended also to include products for export. The application of this strategy was accompanied by a framework of quantitative protection measures, which is organised through import budgets, an administrative pricing system and providing different kinds of promotion and support to enable the national industry to achieve reasonable standards of production. The policies have enabled national industrial production to enter the international market. However, the amount and value of industrial exports are still limited and have not met expectations. Applying this strategy was done in ignorance of a need for the abundance



of foreign currency to support industrial projects (development plan 2001-2005). This also led to the establishment of many industries relying mainly on supplies from foreign markets to fulfil their production requirements. However, all development plans aim to direct national production to rely on local raw materials. The present study aims to understand the impact of imported production requirements on the Libyan private organisations (see Chapters 6, 7, 8 and 9).

Because of world economic change and how this was reflected in the national economy, legislation was applied to pave the way for the stimulation of the private sector and foreign investments. Sklair (1994) stated that two transformations were involved in the process of incorporating Libya into the world economy: first, the transformation of the number of production processes in areas that were integrated into the commodity chain of the world economy, and second, the reconstruction of existing Libyan political structures operating within the interstate system of the capitalist world economy. According to the new thoughts and objectives adopted in the development plan 2001-2005, this plan rested on achieving essential change in the national economic structure. The general strategy of the plan is to activate economic growth, and because of this, industrial sector growth is considered the main motivator for targeted growth. Thus the sector developments rest on the following main principles:

1. Choosing industries that are able to achieve production objectives and encourage these industries to compete in foreign markets by concentrating on reducing cost and improving quality.
2. Replacement of a production strategy based on the proliferation of industries, known as balanced developments, with a concentration on industries (the present research case studies), based on local materials that have the ability to develop as well as to grow.
3. The reorganisation of the industrial sector by reforming public industrial companies financially and administratively and also providing the appropriate economic climate to enable an increase in production. One of the important steps to reform the public industries is to transfer their ownership to the private sector and selected sectors are good examples of this change (see section 5.5).



4. The provision of the requirements for production as well as the supply of spare parts, enabling Libya to achieve the targeted production.
5. The provision of the necessary finances to industry and the promotion of industrial projects and general support of industries (such as Food, Paper and Construction Materials activities) to meet the national demand.
6. The encouragement of foreign capital to participate in joint operations and investments to ensure promotion of the existing Food, Paper and Construction Materials industries and ensure employee training schemes for these activities.
7. Motivating and increasing the number of private factories, in terms of privatization of public sector organisations, which are transferred to the private sector (see section 5.5).

- **The Finance phase**

The financing of development project plans is derived from four sources:

1. Development Banks and the private sector help in financing Food, Paper and Construction Materials factories.
2. Public companies and the government finance certain strategy projects.
3. The Ministry of Finance finances some strategic economic and political projects.
4. Contributions from foreign companies.

- **Policies to achieve the development strategy**

Achieving the objectives of the industrial development plan (2001-2005) required policies that can rectify the limitations of previous industrial development plans and break the dominance of the public sector. The contribution of the public sector industries was very low and in the previous development plans it was one of the main barriers to the improvement of the private sector. The most important policy is to improve and support private enterprises with an emphasis on the industries covered by the research case studies. Several procedures were introduced to attempt to achieve this:



1. a reduction of the productive role of public companies in the field of the small/medium enterprise sector, and the maintenance of its role in heavy industries;
2. a specification of the range of authority between public and private sectors to avoid a conflict of objectives;
3. an improvement of industrial and investment laws to make them suitable for Food, Paper and Construction Materials enterprises and to allow these enterprises to achieve their objectives;
4. an identification of the public companies and factories that are to transfer to the private sector;
5. provision of financial support to finance the Food, Paper and Construction Materials enterprises;
6. emphasis should be given to the private sector in the initial stages by promoting its products in internal and external markets.

In terms of a broad division, the Libyan industrial sector is divided into two sectors: (a) the public sector, which includes all public companies and its branches and is controlled by the state and (b) the private sector, which consists of all medium and small industrial enterprises and the factories that have been privatized from the public sector. For the privatizing of public factories, the General Committee for Privatization was set up to facilitate the financial restructuring by transferring the ownership of 147 public factories to the private sector (see Table 5.3).

### **5.3 The public sector**

The public sector is the part of the country's economic activity that has traditionally been owned and controlled by the government. Basic and processing industries in the country were protected from 1969 to the late 1980s under an incentive regime to promote industrialisation. State enterprises became dominant in basic industries such as energy, telecommunications, water and in processing industries such as oil, soap and sugar. Furthermore, a large (heavy) industrialisation programme began during the 1976-1980 developmental plan. During this plan the capital investment in public sector



manufacturing industries was 1,737 million LD or 24.8% of the total plan investment. The public sector consisted of all public organisations providing most of the community's needs, and was characterised by the heavy involvement of the government (Broadbent and Guthrie, 1992).

The state enterprises have many characteristics. All state enterprises are protected from international competition, no depreciation on the fixed assets is calculated and the accounting surpluses go directly to the state. The responsibility of providing the social subsidies for the employees from 'cradle to grave' imposes a heavy financial burden on public enterprises. The decision-making process in the state-owned organisations flows from top to bottom and the economic information is generated at the bottom level, hence, the quality of the decision-making in most state enterprises is poor in this context. Monitoring and control are centralised at the top. Since 1969 the policy decision-makers have tried to accomplish the objectives of the development plans to:

- improve industry and develop manufacturing;
- end the one-resource principle (of relying on oil);
- become independent from imports and transform the Libyan Community from a consuming community into a productive one.

Since 1969, the industrial sector has gained the support of the Libyan decision-makers. This support started with the establishment of 72 general companies in most of the Libyan regions and the cost of these enterprises was about 5 billion LD<sup>13</sup>. The Industry sector share in GDP increased from 1.7% in 1970 to 6.8% in 1985 (Libyan Industrial guide, 1999, pp.11-12). Since the late 1980s and early 1990s, the public sector on the face of it has lost much of its dominance in Libya, receiving an apparently severe blow with the declaration of a transfer of ownership of a group of public factories to their employees in 1988. Criticism of the public sector had become trenchant and privatisation had emerged as a significant component of public policy.

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<sup>13</sup> LD = around US\$ 2.5.



## 5.4 The private sector and privatisation

*“The solution of all the small public factories’ problems is to transfer the ownership of these factories to their employees”* (The revolution’s leader Moamer Qadafi, 1990)<sup>14</sup>.

Johnson (1988, p.12) stated that, in the British context, the term privatisation “is generally used to mean the formation of a Companies Act company and the subsequent sale of at least 50% of the shares to private shareholders”. The aim of privatisation is not just to sell some shares to private individuals. A significant and relatively invisible aim is to improve industrial performance by increasing the role of market forces. The Libyan privatisation process also has the invisible aim of improving its economy and achieving greater self-sufficiency in particular products such as food, paper and construction materials. For Rapley (1996, p.73) “The severe abuse and inefficiencies often associated with public firms in the Third World provide added impetus to privatization”.

### 5.4.1 Rationale for privatisation

The rationale for privatisation was the assumption that consumers would benefit, directly or indirectly, from the privatisation of the public companies. Beesley and Littlechild (1988) suggest many benefits from privatisation:

- Privately owned companies have a greater incentive to produce goods and services in the quality and variety of the consumer’s preference. Privatisation is intended to change the motivation of management towards profit-making policy.
- A privatised company will be willing to provide economic services.
- The elimination of inefficient production and restrictive labour practices.

A simple definition of privatisation is the divestment of ownership of state-owned enterprises by the transfer of state-owned assets to private ownership in a number of

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<sup>14</sup> Translated into English by the researcher.



ways such as sale, restitution, give-away or liquidation (Bennett, 1997). The common objectives of privatization can be categorised into four groups as follows:

- political targets, such as reducing the dominance of the public sector by expanding the private one and making productive companies more responsive and accountable to those for whom they produce;
- efficiency objectives such as increasing productivity and microeconomic efficiency;
- fiscal stabilisation goals such as maximising the proceeds of sales, reducing the future drain of subventions and capital contributions from government revenue, increasing tax revenues from higher profits and reducing the public debt;
- resource mobilisation goals such as promoting foreign investment in the country and releasing limited state resources for investment in other sectors such as education and health (Bennett, 1997, pp.7-8).

Yet the Libyan experience of privatisation reveals confusion and a contradiction in respect of the first group of the above objectives, which can lead to a lack of clear goals. This contradiction is that in the private Food and Paper factories the government continues to control and supply raw materials, a factor which hinders the factories' competence to achieve, for example, fiscal stabilisation goals (see Chapters 6, 7 and 9). The burden of financing the public sector is admittedly a significant one, although its significance is frequently overstated for political reasons. Advocates of cutting and privatizing public services have a tendency to refer constantly to the level of available resources. In actual fact, it is not just a matter of wealth, but also of how it is distributed, how much of it is raised in taxes and how it is spent, and all these matters are reliant on political decisions. Public services cost money, and few governments have been consistently willing to provide the resources they need (Martin, 1993). Martin (1993, p.38) stated that the public sector has certain failure characteristics:

- a tendency to overstate the extent to which underfunding is responsible rather than confront the thorny issues of management and culture;



- a tendency to excuse poor financial control by stressing the importance of state-owned enterprises in providing employment and meeting social goals;
- a failure by public enterprises to realise their redistribution goals, in some circumstances producing adverse results.

In the case of Libya, some local raw materials are available, and the significant reason for privatising public factories is to achieve the aim of greater self-sufficiency in certain goods by using the available local raw materials instead of being fully dependent on imported goods. In the mid 1980s, because of the drop in international oil prices, the national economy suffered from several difficulties such as the imbalance of the Public budget and a negative Balance of Payments (see Chapter 4). In addition, the depreciation of the performance of public companies played an important role in exacerbating such problems. The public industrial companies were not sufficiently competent to decrease the dominance of the oil industry: their competitive capacity was extremely small and this was aggravated by deterioration in the Balance of Trade. Moreover, the public enterprises constantly reported losses and needed continuing support, which deepened the financial deficit. Therefore, these issues were the major drivers for rebuilding the Libyan national economy in general and the public sector in particular, and providing greater opportunities for the private sector (Privatisation Conference, Tripoli, 2003).

According to the objectives of the Libyan policies and development plans, the Libyan community must be a productive community instead of a consuming one and reduce the domination of public ownership. Small/medium Food, Paper and Construction Materials enterprises are encouraged to play essential roles in helping to:

- develop the Libyan Arab Society;
- improve the working standards in production and service units;
- contribute to the accomplishment of greater self-sufficiency in Food, Paper and Construction Materials.



Financial restructuring policies were adopted to transfer some factories to their employees, including law No. 9 (dated 1985) on the provision related to partnerships. According to this law, the General People's Committee for industry and minerals classified factories into three categories:

1. heavy factories (companies) owned completely by the state and under public ownership;
2. medium sized factories (companies) owned by the state in the form of joint-stock companies;
3. small/medium factories (enterprises), including both existing private enterprises and the public sector factories that have been privatised.

The General Committee for Privatisation established a series of successive executive decrees, starting in 1987, to transfer the ownership of a group of factories to 'the employees'. These decrees specify the mechanism to execute the ownership procedures. According to this mechanism, the procedures were finalized to transfer ownership of 147 state-owned factories distributed in different regions of Libya. Salient information about the public and private factories in different industrial fields is presented in Table 5.3.

According to Table 5.3, the number of these factories and their activities are as follows: 82 factories have been privatized in the Clothing and Textiles sector, equal to 56% of the total number of the factories; 21 factories have been privatised in steel industrial activity (14% of the total number); 17 factories have been privatised in the Food industries' sector (17%); 10 factories in the Paper industry activity (7%); and 7 factories in the chemical industries (4%). There are, in addition, some factories to be transferred in the future (the Libyan industrial guide, 1999, pp.80-81). It is clear from Table 5.3 that small/medium enterprises make up the largest number of enterprises in the Libyan industrial sector. Torbagia (1999) described the increased number of small/medium industrial enterprises as an 'explosion' in the Libyan economy.



Since the 1970s, Libyan policy-makers have become aware of the importance of the Food, Paper and Construction Materials industries. The importance of these industries is that they are the main basis for industrial development, and the policy-makers have aimed to improve and promote them. Construction materials industries also help consolidate integral relations with the national economic sectors<sup>15</sup> (The Libyan industrial guide, 1999).

Table 5.3: The number of factories by industrial sector in 1998.

Kind of activity	Private sector <sup>16</sup>		Public sector <sup>17</sup>	Total
	Existing private factories	Privatised factories during 1988-92		
Food Manufacture	210	17	62	289
Clothing/ Textile	766	82	42	890
Chemical Industry	861	7	35	903
Construction Materials	732	10	63	805
Steel Industry	1,522	21	54	1,597
Paper Industry	1,011	10	20	1,041
Total	5,102	147	276	5,525

Source: the Libyan industrial guide, 1999, Tripoli

Food, Paper and Construction Materials factories have been privatised in light of the importance of these industries as a part of the industrial development plan (2001-2005). This research will focus on the Food, Paper and Construction Materials industries sectors by selecting one case from every sector for conducting the empirical work in order to achieve the research objectives (see Chapter 1).

In light of the above, this research aims to explore and understand the current MCSs in the Food, Paper and Construction Materials industries within their developmental context (see Chapters 6, 7 and 8).

<sup>15</sup> By exploiting available raw materials, providing basic revenues for other industries and sectors and indirectly affecting the improvement of the intellectual and cultural level of Libyan society.

<sup>16</sup> Mainly small/medium companies.

<sup>17</sup> Mainly large companies.



## 5.5 Summary

It can be concluded that Libya at the time of the revolution was very far from having started substantive industrial development. The lack of any broad educational background, the small size of the labour force and the low participation of women in the industrial process put Libya in a disadvantageous position in terms of initiating industrialisation. Consequently, the country remained in a position of dependency on both oil income and foreign human resources for many years. It was only in the late 1970s that the industrial sector became the main target for industrial planning. In respect of resource allocations, development plans show that a huge amount of resources was orientated to improve the industrial sector, which was far from the situation in the revolutionary period. This considerable resource support for the industrial sector reflects the political emphasis this sector has received.

In the 1980s, the government changed its focus to pay more attention to the private sector by making the decision to privatise a group of public factories to their employees. This step was one of the development plan targets to liberate Libya from foreign dependence on 'oil rent' and to strengthen diversified and intermediate production. The transfer of ownership to the private sector was aimed to have beneficial effects on managerial incentives and industrial performance where product markets are competitive and reasonably free from other externalities. The Libyan industrial sector is affected by its environmental circumstances and, therefore, a better understanding of these circumstances within the wider socio-economic and political context is required to understand the processes of any selected organisations in this research. The Food, Paper and Construction Materials sectors have been chosen from the transferred group as case studies, in order to gain an in-depth understanding of the MCSs within their environmental developmental context. The following chapters present the findings of the case studies conducted in the course of this research.



## **Chapter 6: Case No. 1**

### **A Discussion of the MCSs in the Libyan Fallah Factory**

#### **6.0 Introduction**

The main aim of this chapter is to describe and discuss the existing MCSs of the Libyan Fallah Factory (hereafter, LFF). The previous chapter highlighted the Libyan industrial sector in general and private sector in particular. In order to achieve the aim of this chapter, the following aspects of the factory are described: an overview of the factory's history and objectives; the factory's management and structure; the accounting information system; the budgeting system; the cost and pricing system; the accountability system; the manufacturing processes, taxes and custom duties; the factory's effectiveness; a summary of the chapter.

#### **6.1 An overview of the factory's history**

The factory was established as a company in 1969 and continued under the governance of the Public Sector up to September 1<sup>st</sup> 1988, when it was privatised, with ownership shifting to those who were working in it and is now part of the Private Sector. The factory began its operations in the private sector within certain legal requirements<sup>18</sup>.

The designed productive capacity of the factory was 16,400 tons of pear juice per year and the targeted production was 13,700 tons per year. Moreover, in 1994 a new line for pear juice production was established with a production capacity of 15 tons of juice per hour (15 x 10 hours x 280 working days = 42,000 tons per year). On 15<sup>th</sup> June 2001 a new line for the production of sliced chipped potatoes was established and is now under experimental operation. This line is likely to succeed since there are sufficient supplies of potatoes nearby. The factory is also capable of producing all kinds of juices such as

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<sup>18</sup> Licence No. 355, Commercial Register No. 915, Taxation Register No. 1076 and Social Security Register No. 1530000494.



orange, lemon, grape, peach and apple, and is also capable of producing canned olives and peppers. The raw materials for all these products, except for the oranges and olives (but even these are dependent on the success of the agricultural season), are not available locally.

Since its establishment and development in 1994, the main product of the factory remains pear juice and the raw materials are imported from Australia, which has the best quality of pears in the world market. The factory is capable of competing in the world market because of its high quality products and its being subject to international quality standards in the world markets (some Italian experts have audited the factory for quality control purposes).

#### **6.1.1 The objectives of the factory**

The short and long-term targets of the factory are to increase its productive capacity to meet the ever increasing demand for food products and the production of all kinds of juice with the participation of all employees in the productive efforts. The material and moral life of the employees will also improve as a result of the returns from effort exerted, and from the fact that the employees will feel that they are the owners of the factory, at least partly (the ownership contract, article 2). The Secretary of the People's Committee (manager) of the factory emphasised that:

“The privatisation of the factory to the employees is a revolution in terms of the benefits for them. These employees were previously paid for their work in the form of a monthly salary while working for others, whether public or private companies. However, after privatisation, the employee is working for himself, and the profits now go to himself, his family and the society through the provision of important foodstuffs for all members of the community”.

The Director of Financial and Administrative Affairs described this process as one which offers very strong incentives for increasing production and the improvement of the employee conditions inside the factory. It is also a step towards self-sufficiency in food materials. He continued:



“Since the factory has been owned by the employees, the production has increased almost three times, profits have increased, there has been an improvement in the condition of the employees. Part of the profits has been allocated to improvement and replacement of the factory assets. In 1994 a new production line was established, and the factory became the third biggest factory for food products in Libya and Italy”.

## **6.2 Factory management and structure**

This section is divided into two parts: the first part examines the relationships between the factory’s management and its environment and the second considers the internal relationships between the management and the other parts of the factory (see Figure 6.1).

### **6.2.1 The management and its external environment**

The nature of the relationships between the factory and the Tripoli municipality bureaucracy (e.g. Ministries) is probably not clear cut and lacks a smooth flow of information. The reason for this could be the absence of clear and official procedures to show the nature of the relationship between the factory and the state bodies such as the Ministry of Industry. Simultaneously, a direct relationship exists between the factory and the Ministry of Industry of the Tripoli municipality, as the factory fell under the supervision of the Ministry of Industry only after its privatisation whereas before the factory used to be a part of the latter. The Ministry of Industry still plays a significant role in the daily production processes within the factory by involving itself in the administrative affairs and production policies of the factory. Moreover, it attempts to impose certain regulations, which do not form part of the privatisation contract. Obvious examples of this interference are in the product pricing policy and the import budgets (see sections 6.5 and 6.6). The reason for this interference seems to be a result of a lack of clear rights, duties and responsibilities of the personnel of the Ministry. An example of this interference is the influence on the appointment of the chairperson of the People’s Committee in the factory; this shows the Ministry exerting a direct influence on the factory’s activities through informal procedures as the Ministry of Industry has effectively appointed the factory manager.

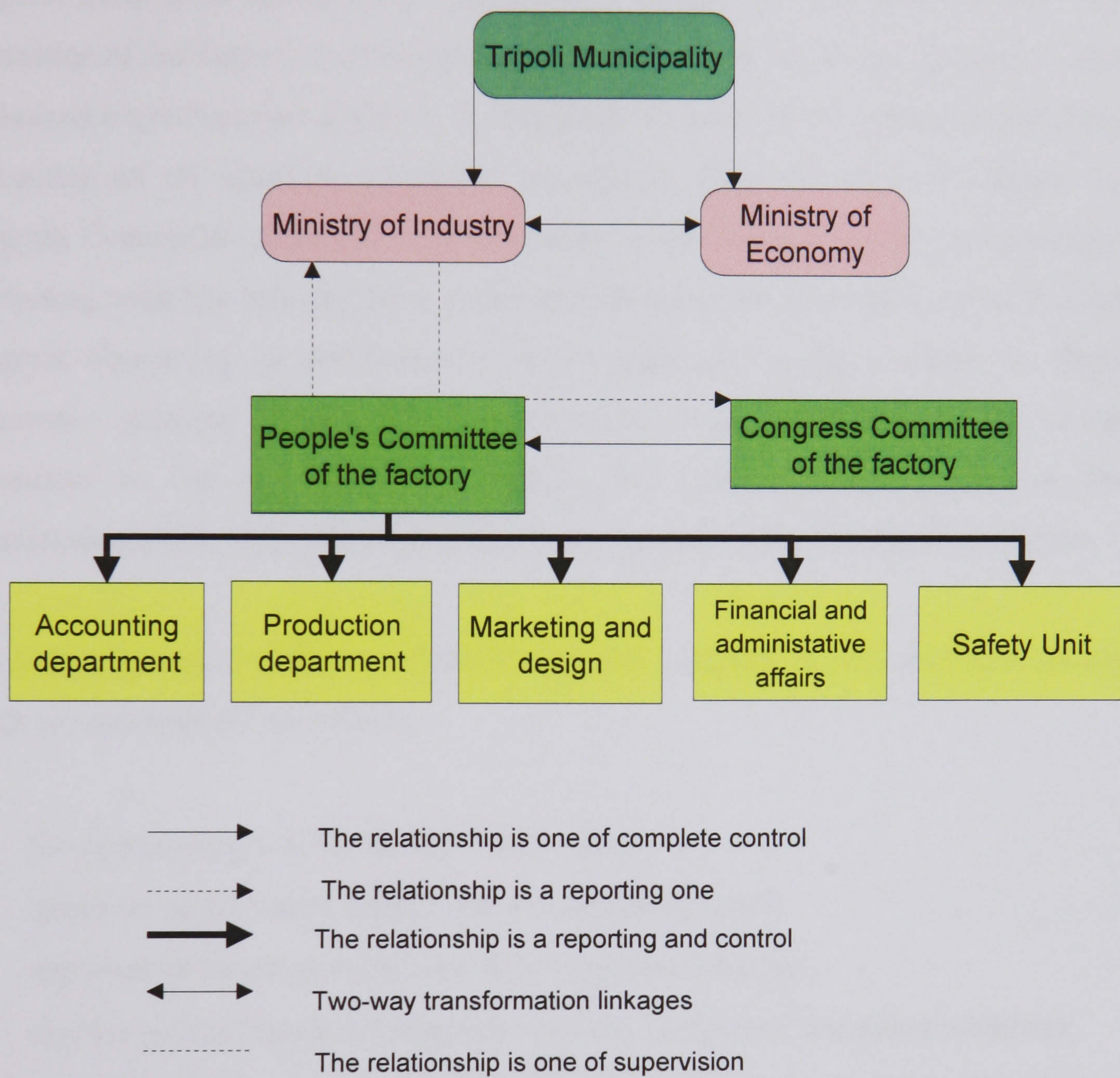


It can be concluded that the Ministry of Industry still plays a significant role in controlling the day-to-day processes in the factory and that the role of the actual factory's management in managing and controlling its activities seems to be restricted and done under external influence. Consequently, there is a degree of conflict and contradiction with the written rules and policies, as the written rules emphasise that the management has the right to manage and control the factory independently in real situations. One of the important causes of this conflict may be that people in the Ministry of Industry still think that the factory is a state-owned factory. Also, this kind of intervention leads to minimising the role of accounting information regarding these areas (cost, pricing and budgeting functions) as personnel in the factory do not pay attention to the importance of this information in their decision-making process because decisions regarding these areas have been made externally (in the state ministries) (see Chapter 9).

### **6.2.2 The management and its internal environment**

The management of this factory consists of five people acting as a People's Committee, with a chairperson and four members. The chairperson is called the Secretary of the People's Committee. This committee is elected by the employees to manage, control and plan the activities of the factory with a view to achieving the factory's objectives. This committee has an administrative staff to undertake and control day-to-day jobs such as financial processing, computing, budgeting, banking, inventory control, product control and pricing. A set of written rules, procedures and policies in the privatising contract are used to guide People's Committees as they administer their departments (see Figure 6.1 and Appendix A). All employees are members of the Productive Congress, which meets at least once a year and sometimes more often according to the situation of the factory and its activities. The Productive Congress elects both the Congress Committee and the People's Committee.





**Figure 6.1: The structure and the communication and control linkages in LFF.**



According to the contract of ownership, the Productive Congress represents all the employees in the factory (every worker is a member of the Congress) and each employee holds the same number of shares in the factory. The Productive Congress elects the People's Committee and the Congress Committee of the factory. The Congress Committee represents the Productive Congress as a controller of the People's Committee of the factory to ensure that the latter executes the factory's plans to achieve the desired objectives (see Figure 6.1). The People's Committee reports to the Congress Committee on all activities conducted through its administrations. It reports to the Congress Committee about the control process in the form of a report comparing and contrasting what has actually been achieved with the goals previously set as Productive Congress objectives. In addition, in order to attain day-to-day control, the People's Committee presents copies of all its decisions and resolutions to the Congress Committee so that the latter may identify any deviations from policy or poorly administered procedures that might have been enacted by the People's Committee.

The annual general conference of the Productive Congress covers a number of issues, which are summarised as follows:

- the annual report of the factory's activities;
- approval of the balance sheet and the income account;
- approval of the proposal for the following year's budget;
- election of the People's Committee and the Congress Committee members;
- the final election of the People's Committee members does not take place until the Ministry of Industry of the municipality has confirmed and accepted the election of those members. People's Committee membership is valid for five years.

The People's Committee of the factory has many additional duties for managing the factory:

- preparation of plans and programmes to achieve the factory's objectives;



- preparation of the budget proposal for the following year and the budget of the current year;
- provision in respect of the buying of all the production process needs such as raw materials, and spare parts;
- control and improvement of product marketing;
- preparation of training programmes for the workers.

From Figure 6.1 it can be seen that the relationship between the People's Committee and its administrative departments is one of management and control. The Production Congress of the factory draws up the policies and rules through which it is hoped the People's Committee will attain the factory aims and objectives. All departments are directed by the People's Committee to reach these goals. In addition, all departments correspond with the People's Committee concerning any departure from or contradictions between policy and practice until the source of these contradictions is identified and remedied so any mistakes can be avoided. This helps to maintain co-ordination between the system units. The Productive Congress is invited annually by the Congress Committee to the factory's general meeting for the presentation of the annual report of the factory's activities. In this accountability and assessment meeting, the People's Committee presents a detailed report about all activities in the factory and what it has achieved in the past financial year and highlights all operations and proposals for the coming year. Also in this meeting, the financial accounts are reviewed and inspected for approval. The Productive Congress also has the power to convene to replace any member of the People's Committee or the Congress Committee and approve any changes in the plans or policies of the factory (see Appendix A).

From the written rules and policies the Productive Congress has the right to replace and appoint any member of the People's Committee or the Congress Committee at any time. However, the actual process is complicated as this kind of process needs approval from the Ministry of Industry. Furthermore, the Ministry of Industry has on many occasions become involved and appointed the chairperson of the People's Committee.



### **6.3 The role of the accounting system**

The Head of the Accounting Department has suggested that accounting information plays a vital role in the decision-making process. The accounting system continues to provide information to the management and other external parties such as the Ministry of Industry. This information consists of items such as the cost of imported and local materials, the financial figures with regard to cash flow to be used in decision-making for future imports and determining the cost of production. Management is also provided with information and statements, which help in comparing the budgeted materials used in production, and the actual production, so as to avoid any future deviations. This comparison encourages the producers to increase their awareness about the importance of the raw materials as inputs for production. This process also aims to achieve control on the final product to prevent misuse and/or spoiling of the product components.

The Director of Financial and Administrative Affairs argued that all these features became very clear after the factory had become private. The producer (employee) became more attentive to understanding the costs and how to reduce them to achieve high returns. This accounting awareness has also increased among the producers and managers, and every producer now pays more attention to using better means of production and methods to control the use of raw materials and avoid any misuse of materials.

The Head of the Accounting Department (who has held this position since 1986) emphasised that the accounting awareness and the care for expenditure and proceeds had increased to a great extent among the producers since the time of privatisation. With regard to the changes of the accounting system, the Head of the Accounting Department mentioned that before privatisation the accounting system was limited to the preparation of income and the general budget only. However, since privatisation, the operation of marketing was added to the accounting system and the factory became responsible for the administration and marketing operations. It also became responsible for the preparation of costs, dealing with customers and collection of debts. Before



privatisation all these functions were carried out by a General Committee of the state under the auspices of the Ministry of Industry. The concern and target of the employees before privatisation was just to work from 9.00 a.m. to 2.00 p.m. as their salaries were secured by the state. Their salaries were not paid through the factory's administration but were prepared in the accounting department and paid by another authority. Now there are accounts for the banks, cash, sales, debtors and creditors and these functions need more accounting information in order to be fulfilled successfully. The Director of Financial and Administrative Affairs said that all the information and statements needed for decision-making with regard to costs of raw materials, costs of production and stock were available on time. One of the accountants stated that the relationship between the accounting department and the factory's management is a direct one. On many occasions, some accounting information about the activities of the factory is requested by the management or by part of the factory and is immediately available.

The Director of Financial and Administrative Affairs noted that the accounting system in the factory was very effective. Indeed, this is evidenced by the operational budgets being prepared on time every year and presented before the state authorities (Ministry of Industry) request date of July the 31<sup>st</sup>. Most of the final accounting statements are prepared without any difficulty for the appropriate deadline for all those who need such statements and who request them to be sent to them. There are no outstanding debts or liabilities against the factory. The Director of Financial and Administrative Affairs continued:

“I did not need to look into the accounts records and documents since I used to store 80% of the important information in my memory. The only problem we had was that the computer facilities were not introduced in our accounting system processes. We managed to overcome this partially by using a salaries' software, which is now working very satisfactorily and saves a lot of time and effort”.

As with any other developing systems, the accounting system needs time before the accountants and producers are convinced of the computer's efficiency in executing accounting processes in a shorter time and that it is not meant to replace them but help them. The Director of Financial and Administrative Affairs pointed out that “we used to



work out salaries over several weeks; now we do it in two days and correct mistakes and additions promptly on the computer instead of retyping them.”

The Head of the Accounting Department stated that the general idea of the Libyan privatisation process was to distribute the returns equally between the employees. However, the accounting process and calculations of the profit distribution inside the privatised factories were done differently. There were factories, which were applying the policy of equal return distribution between the employees, while others apply the salary system of law No. 15 of 1981.

The Head of the Accounting Department continued and explained that the system applied in this factory is as follows: for instance, the Manager of the factory receives a salary amounting to 400 LD per month. According to the points system, each point is equal to 10 LD. Thus, the total number of his points is 40 (400LD/10LD) points. From this total any absence or non-conformity with the organisation of the factory is deducted, absence for one day being equal to one point. At the end of the year, when deciding on the annual income to be distributed among the producers, each producer is allocated the number of his points after the reduction of points for absence and non-conformity (such as late arrival at work). The income liable for distribution is calculated from the total points for each producer, and each producer receives his share of the profit according to his net points. The Head of the Accounting Department explained that since 1999 the factory has not achieved any profits because of extraneous circumstances such as the lack of raw materials, the lack of foreign currencies, shortage of loans and the fixed state procedures<sup>19</sup> regarding the import of the factory's needs. From the analysis of the factory's documents it appears that 1999 was the last year that the factory achieved a profit (see Tables 6.1, 6.2, 6.3).

From the structure and the design of the income accounts in the Tables below, it appears that the accounting department in the factory still uses the British-influenced accounting system. This is understandable, as both the Head of the Accounting Department and the external accountants were educated in UK universities.

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<sup>19</sup> The high taxes and customs imposed on the privatised factories.



حسابات النتيجة عن الفترة من 1999/1/1 الى 1999/12/31 ف

بيان	المبلغ		بيان	المبلغ	
تكلفة انتاج الفرة	2256123	296	ح/ التشغيل :- خدمات رئيسية خدمات مساعدة مواد تعبئة وتغليف المرقات والاجور الاستهلاكات الصناعية المصروفات الصناعية	564036	633
	2256123	296		1878	025
المبيعات	2720587	500	ح/ المتاجرة :- تكلفة انتاج الفترة انتاج تام اول المدة	1061481	481
	13265	800		362619	748
انتاج تام اخر المدة / عصير كمشري	19536	000	مجم	227098	508
انتاج تام اخر المدة / عصير عنب	598	000		39008	901
انتاج تام اخر المدة	2755987	300	ح/ الارباح والخسائر :- المصروفات العمومية استهلاكات ادارية صافي الربح	2256123	296
مجم	499266	004		166243	914
الادوات متنوعة	2000	580	تكوين مخصص ضريبة الشركاء صافي الدخل بعد الضرائب	3371	120
صافي الدخل قبل الضرائب	501266	584		331651	550
	331651	550		501266	584
	331651	550		112841	052
	331651	550		218810	498
	331651	550		331651	550

\* صافي على صر  
\* محاسب / جميع قانوني  
طرابلس / الجمهورية

حلى

Figure 6.2: The Income Account of the LFF for the year ended 31/12/1999.



Table 6.1: A translation of the Income Account of the LFF for the year ended 31/12/1999.

Particulars	Amount (LD)	Particulars	Amount (LD)
Operations account:			
Main raw materials	564,036.633 <sup>20</sup>		
Support raw materials	1,878.025		
Packaged materials	1,061,481.481		
Wages	362,619.748		
Industrial depreciation	227,098.508		
Industrial expenses	39,008.901		
The product cost in the present period (1)			2,256,123.296
	2,256,123.296		2,256,123.296
Commercial account:		Sales	2,720,587.500
The product cost (1)	2,256,123.296	Finished products	
Finished product at 1/1/99	598.000	at 31/12/99	33,399.800
Gross profit (2)	<b>499,266.004</b>		
	2,755,987.300		2,755,987.300
Profit and loss account:			
Administration expenses and depreciation	169,615.034	Gross profit (2)	499,266.004
		Sundry proceeds	2,000.580
The net profit (3)	<b>331,651.550</b>		
	501,266.584		501,266.584
Producers taxes reserve (4) <sup>21</sup>	112,841.052		
Net profit after taxes (3-4)	<b>218,810.498</b>		

Source: the factory’s final accounting statements, Tripoli, 1999.

<sup>20</sup> 1 LD = 1000 Derham.  
<sup>21</sup> This is an estimate of the tax liability.



### حسابات النتيجة من الفترة من 2000/1/1 إلى 2000/12/31

\* محمد علي باشا \*  
 معاليه و مدبره  
 طرابلس / ١٢٨٥

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Table 6.2: A translation of the Income Account of the LFF for the year ended 31/12/2000.

Particulars	Amount	Particulars	Amount
<b>Operation account:</b>			
Main materials	321,967.890		
Support materials	1,789.251		
Packaging materials	623,454.594		
Wages	201,706.044		
Industrial Depreciation	226,466.447		
Industrial expenses	45,471.875		
The product cost in the present period (1)			1,420,856.101
	1,420,856.101		1,420,856.101
<b>Commercial account:</b>			
Product cost (1)	1,420,856.101	Sales	1,404,048.645
Finished product at 1/1/2000	35,399.800	Finished product at 31/12/2000	88,622.400
Gross profit (2)	<b>36,415.144</b>		
	1,492,671.045		1,492,671.045
<b>Profit and Loss account:</b>			
Administration expenses and depreciation	162,209.045	Gross profit (2)	36,415.144
		Damaged finished products	3,822.966
<b>Net loss</b>			<b>121,971.553</b>
	162,209.663		162,209.663

Source: the final accounting statements of the LFF, Tripoli, 2000.



### 6.3.1 The accounting year

#### The Income Account

Table 6.3: the Income Account for the year ended 31/12/2001.

Particulars	Amount	Particulars	Amount
<b>Operation account:</b>			
Main materials	339,480.174		
Support materials	1,851.995		
Packaged materials	674,670.528		
Wages	458,674.322		
Industrial depreciation	227,320.147		
Industrial expenses	29,442.020		
The product cost in the present period (1)			<b>1,731,439.086</b>
	1,731,439.086		1,731,439.086
<b>Commercial Account:</b>		Sales	
Product cost (1)	1,731,439.086	Finished product at	1,695,352.250
Finished product at 1/1/2001	88,622.400	31/12/2001	76,698.600
Total loss (2)			<b>48,010.636</b>
	182,0061.486		1,820,061.486
<b>Profit and loss account:</b>			
Total loss (2)	48,010.636		
Administration expenses	187,278.709		
Bad debts	307,186.308		
Administration depreciation	4,316.266		
Net loss			<b>546,791.919</b>
	546,791.919		54,6791.919

Source: the final accounting statement of the LFF, Tripoli, 2001.



### 6.3.1 The accounting cycle

The accounting applications pass through two stages, the documentary phase and the book phase. The documentary phase of the imported raw materials is considered the most important phase in the factory and its generation is now described. A record for funds is opened when an approval is given by the Ministry of Industry, and an analytical record is then opened for the fund showing the amount, the place of import, the value of the fund and time of arrival of the raw materials. Next, a committee is formed to receive the raw materials from the Customs Department; this Committee then compares the specifications of the raw materials with those in the invoice and prepares a record of inspection and an identical record for these materials with regard to quantity and quality. This committee then prepares a handing-over record for the storekeeper in the factory. The latter should prepare a submission for additions to the stored materials to be sent to the accounting department to prepare the daily registers and compare each category of raw material. With regard to the book record and according to the Libyan Commercial Code, each institute, public company or private company, should have at least a daily general record containing the following main accounting details: The cash in hand, the cash at bank, the debtors, the creditors, the sales, the purchases, the loans, insurance, securities and the assistant ledger such as analytical accounts. For the final accounts, the profit and loss account and the balance sheet are required.

There is no separate section for the cost accounting and the cost of the production elements is prepared by an accountant<sup>22</sup>, and the final accounts are prepared before July 31<sup>st</sup> each year. These accounts are presented to the Ministry of Industry for discussion and approval. The management of the factory seeks the assistance of an external auditor to prepare and audit the accounts using the most effective methods and all necessary documentation and a draft of the final accounts are presented to the external auditor (Libyan professional accountant) to help in preparing the final accounts in the most appropriate way before their being submitted to the Ministry of Industry. The Director

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<sup>22</sup> This person is a general accountant without any formal professional qualifications. It is common practice to employ such accountants in Libyan industrial sector.



of Financial and Administrative Affairs referred to the lack of sufficient experience of the factory accountants by saying:

“The preparation of the final accounts takes quite a long time and many mistakes are noted, which need correction because of the lack of a proper orientation with the accounting processes. This is why we resorted to the external accountant who is well experienced in taxation and final accounts preparation. Several times he succeeded in solving outstanding problems with the department of customs”.

It can be concluded that the role of the accountant is only a routine job, which is to ascertain the figures of the invoices of the accounts. Also the role of the internal auditor is to examine the invoices and compare their values with the cheques.

## **6.4 The budgeting system**

The Head of the Accounting Department stated that from privatisation (in 1988) up until 1995 the production circumstances were very favourable and the Libyan market was stable. There were no surplus stocks of products and there was an increase in local demand for the products of the factory. This stability engendered a degree of certainty and explained why, (in the opinion of people in the factory), annual budgets were prepared for all the factory's activities. The actual production was matched with the estimated production and all divergences were calculated and taken into account to avoid them in the future plans.

From 1998 up to the time of this research, several problems were faced by the factory: market instability; difficulty in obtaining the quantities of the raw materials needed by the factory as the state controlled them; the strict control on foreign currency imposed by the Ministry of Industry. All these factors made it quite difficult to prepare estimated budgets since it was not easy to make any firm estimates regarding the production or sales, or any other factors because of the stagnant market, and inability of the local products to compete with the imported products owing to the high cost of raw materials and spare parts. In 2001 the government stopped supporting privatised factories by ending the allocation of foreign currencies and by the flotation of the Libyan Dinar. The U.S Dollar was worth 0.30 LD but now it is equal to 1.6 LD (see Table 6.4). The Head



of the Accounting Department mentioned that all these factors contributed to making it difficult for any organisation to forecast the future. Hence, the preparation of budgets became ineffective and this is why the operational budget is sometimes the only budget that is prepared, either for legal purposes, or to satisfy certain public agencies such as the Ministry of Industry.

Table 6.4: The exchange rate between the US\$ and the Libyan Dinar.

Year	Foreign currency	Exchange rate
1990	1 US\$	0.270 LD
1991	1 US\$	0.270 LD
1993	1US\$	0.300 LD
1996	1US\$	0.450 LD
1998	1US\$	0.600 LD
1999	1US\$	0.600 LD
2002	1US\$	1.600 LD*

\* Since the last quarter of 2002 the Libyan Dinar has been floated and the US\$ has become available everywhere.

Source: The Central Bank of Libya, Tripoli, 2002.

The Director of Financial and Administrative Affairs at LFF described the process of preparing budgets as follows:

“[T]he preparation of the budgets during the present period is useless since there is no possibility for estimating any factor of production cost, because of the lack of information or data about those factors and surrounding circumstances. There are no indexes or rules to predict the local market, therefore, the preparation of the budgets is just being done as routine and we will stop it soon”.

Therefore, the preparation of budgets is limited to the preparation of the import budget so as to determine the requirements of the factory from imported raw materials, machines, and spare parts. (These are items that determine the foreign currency needed by the factory for imports). Yet even this budget was done as a routine process only to satisfy the requirements of the public entities such as the Ministry of Industry.



The factory is in fact given only a small part of its estimated requirements and this is reflected in its productive capacity: only 200,000 tins were produced per year (only about 10% of the total productive capacity), whereas the productive capacity of the factory is 500 tins x 60 min. x 10 Hrs daily x 280 working days = 2,100,000 tins. Table 6.5 shows the annual requirements approved from the total import budget.

Table 6.5: The import Budget of 2002 (US Dollar).

Name	Unit	Quantity	Price US\$	Total US\$
Pears	Ton	2,127	720.00	1,531,440
Flavour	Kilo	500	3.52	1,760
Citric Acid	Kilo	1,500	1.30	1,950
Ascorbic Acid	Kilo	3,100	4.90	15,190
Cans (170gm)	Tin	80,640,000	0.06	4,838,400
Cans (500gm)	Tin	200,000	0.095	19,000
Cans (5kilo)	Tin	15,000	0.64	9,600
Carton	Item	<u>2,100,000<sup>23</sup></u>	<u>0.11</u>	<u>231,000</u>
Total				US\$ 6,648,340
US\$ allocated in 2002				US\$ 600,000
Shortfall				US\$ (6,048,000)

Source: Factory financial statements, Tripoli, 2002.

The Secretary of the People’s Committee said that it was not only the insufficiency of foreign currency that was restricting the production, but also the complexity of the procedures that have to be followed to secure the funds. The approval of imports would normally be given in November while the procedure for securing the fund may take more than three months. This may sometimes reduce the ability of the factory to make full use of such funds because the validity of any fund is terminated by the end of the state financial year on 31/12. The Secretary of the People’s Committee described the procedures for achieving the import raw materials by saying that:

<sup>23</sup> This figure is by coincidence the same as the productive capacity of the factory shown above in Table 6.5.



“In 2001 the approval was given in November. Procedures started forthwith to make use of the fund. The documents were sent to the Central Bank on December 30<sup>th</sup>. The money was credited to our account, using all kinds of support and our personal relations to complete the process on 31/12. If we had been late by only one day we could have lost the whole budget of 2001”.

The Director of Financial and Administrative Affairs explained that the relationship between the factories and government before and after the privatisation was slightly different. For example, the budgets for imports were very high before the privatisation of the factory, but now the factory receives only about 10% of its required budget. Furthermore, the Director of Financial and Administrative Affairs stated:

“I sent a verbal claim to the Minister of the Industrial Sector when we received only a small portion of our actual needs. The Minister of the Industrial Sector replied ‘go on, execute your budget before you lose it, we are in a state of siege, which may not permit the discussion of such issues’”.<sup>24</sup>

In addition to the above, the Director of Financial and Administrative Affairs argued that there are problems with administrative procedures such as payment of taxes and customs, which prior to privatisation did not pose any problems. For the Director, nowadays, the Government considers private factories as its ‘enemy’, and hence, shackles or restricts everything through handicaps and constraints in spite of the fact that these factories have provided employment opportunities for the Libyan people and saved the state from having to raise funds for hundreds of Libyan families.

## **6.5 Cost and pricing system**

The cost and pricing system at the LFF is not very different from those in other factories, since one authority (the Ministry of Economy) fixes final prices for all products. One of the accountants said that he prepares the statement of the final costs of the product by calculating the direct and indirect costs. After calculating the final product cost, it is sent, with an official letter, to the pricing department in the Ministry of Economy in Tripoli Municipality which determines the sales price to the consumer

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<sup>24</sup> This Minister’s reply referred to the UN economic sanctions.



and to the public institutions<sup>25</sup> or through any other channels of distribution. The final cost of the product includes several expenses such as production taxes and customs. The former is an additional burden for the factory, especially under the present situation of the accumulation of the local production and low demand owing to high production costs. One of the accountants argued that “the Ministry of Industry imposes 10% as production tax on the factory even if the factory is unable to sell one unit of its production due to the high cost of production, so this is unjust.”

The Director of Financial and Administrative Affairs argued that the solution is not in adjusting the margin of profit, rather, it is in reducing the cost of production. Anderson and Lanen (1999, p.401) stated that “cost reductions in manufacturing are important to the future of the company.” Cost reduction in Libyan factories cannot be attained without giving these factories some exemptions from taxes and fees so that they can charge competitive prices against comparable imported products. The Director of Financial and Administrative Affairs asserted that “85% of the product cost is income tax, production tax and customs duties. Hence the factory has no chance to reduce this burden without a Government resolution, since these are considered statutory fees.” As a result of these high duties and taxes, the cost of the product is very high and the competitive capacity of the factory very limited. For example, the total cost of producing a packed box of pear juice 40 x 170 gm is 13.295 LD; however, the factory sells it for 10.50 LD (because of the low price of imported products) (see Table 6.6). Consequently, the factory is selling its product at a loss, just to cover its daily expenses. In addition, the demand for products is still low as there are cheaper imported products in the market. Indeed, the Secretary of the People’s Committee referred to the fact that there are many factors that make the imported products cheaper than the local products, the most important of these being the misuse of the Trade Agreements between the Arab countries and Libya. These agreements are changed in what could be argued to be an unjust form of competition. This happens thus: cheap products are imported from East Asia or from Europe by people bringing them and claiming that these products are from the Arab countries so they are exempted from customs duties. This has a negative impact on local production. A further factor is the problem of the high exchange rate,

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<sup>25</sup> All public institutions such as schools and hospitals.



especially between the US Dollar and the Libyan Dinar. The high increase in the exchange rate from 0.300 LD for one US\$ to 1.5 LD has resulted in price increases for all imported production materials. Therefore, all costs of imported production materials have increased and the financial burden on the factory of securing the elements of production is transferred to the consumer, who is in actual fact supposed to be the beneficiary of the policies. Table 6.6 shows the cost of producing a box of pear juice according to the new exchange rate:

Table 6.6: The cost of producing a box of pear juice according to the new exchange rate.

Cost elements	The cost of packed box 40cans x 170gm	US Dollar
Raw materials	4.142 LD	2.761
Packed materials	6.118 LD	4.079
Wrapping materials	0.280 LD	0.187
Total of the materials cost	10.540 LD	7.027
Assets depreciation	1.527 LD	1.018
Industrial expenses	0.157 LD	0.105
Industrial wages	0.423 LD	0.282
Total of direct expenses	12.647 LD	8.432
Administrative expenses	0.648 LD	0.432
Total cost	13.295 LD	8.864

Source: the factory financial statements, Tripoli, 2002

### 6.6 The accountability system

Monthly or quarterly reports are prepared on the production and the problems faced by employee-owned factories. These reports are sent to the Ministry of Industry in the Tripoli Municipality for the supervision of these factories. The Secretary of the People’s Committee of the factory explained that monthly reports were sent to the Ministry of Industry which sometimes sent supervisors to ensure that all statements given in the report were correct and also to note any short-comings and problems in the factory.



However, these operations had become very limited or even ceased after the state stopped supporting these factories and curtailed the provision of foreign currency for imports in 2000. At the factory level, the Congress Committee normally convenes some sessions of the Productive Congress, which embodied all the procedures to discuss matters and arrive at some solutions. Monthly meetings are also held and convened between the People's Committee and the Congress Committee, in these meetings production problems associated with the daily work are discussed and solutions suggested to avoid such problems in the future (according to Secretary of the People's Committee). The director of the privatised factories department in the Ministry of Industry stressed that the accountability process should be carried out inside the factories in the Productive Congresses as the role of the Ministry of Industry is only supervisory.

The overall objective of transferring the ownership of these factories from the public domain to their employees is that they are controlled and run by the private sector only. The researcher's inspection of the reports of meetings held in the factory revealed that no single responsibility was attached to any person or authority or section in the factory and all were just routine meetings that were held every month or every three months. In these meetings, the Secretary of the People's Committee elaborated all the problems faced by the factory, especially those related to production and the attempt to find solutions for these production related problems, yet no person in the factory shouldered the responsibility of such problems.

## **6.7 Taxes and Customs Duties**

Taxes and custom duties on the imported raw materials and spare parts pose the most significant constraints. These are the most serious problems the factories face, making them unable to compete in the open economic atmosphere at present dominant in Libya. With regard to the customs laws and regulations for imported goods such as those manufactured in some Arab and African countries, and according to the Economic Agreement signed between Libya and some countries such as Egypt, Tunisia and Sudan, all products coming from those countries are free of customs excise duties. However, Libyan privatised factories receive their imported raw materials and spare



parts at high customs and taxes rates, which may amount to 85% of the value of the invoice in some cases (see Tables 6.7 and 6.8).

Table 6.7: A translation of the taxes and customs fees on imported raw materials (tins).

Particulars	Amount
Bank commission	1,965 LD
Bank expenses	5,160 LD
The Great Man-made River tax 15%	156,840 LD
Custom expenses	7,455 LD
Navigation expenses	41,380 LD
Harbor dues	38,893 LD
Transportation expenses	27,900 LD
General fees	2,500 LD
Marine insurance	1,195 LD
Printing fees 8%	<u>83,648 LD</u>
Total expenses	<u>366,936 LD</u>
Total credit for import	<u>1,045,606 LD</u>
The percentage of expenses	35%
Production tax	10%
Bank interest	<u>7.5%</u>
Total	52.5%

Source: The accounting statements, Accounting Department, Tripoli, 2001.



شركاء لأجراء



الجمهورية العربية الليبية  
الشعبية الاشتراكية العظمى  
اللجنة الشعبية للصناعة  
مصنع الفلام الليبي للمنتجات الغذائية

التاريخ / /  
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الرقم الاشاري

### إعتماد علب الصفيح

قيمة الإعتماد بالعملة الصعبة 1.733.160.000 ليرة إيطالية

قيمة الإعتماد بالدينار الليبي 1.045.606 د. ل

1.965 د. ل	◆ عمولة المصرف
5.160 د. ل	◆ مصاريف أخرى للمصرف
156.840 د. ل	◆ النهر الصناعي 15 %
7.455 د. ل	◆ مصروفات جمركية
000	◆ رسوم جمركية معفية
41.380 د. ل	◆ مصروفات ملاحية
38.893 د. ل	◆ مصاريف مواني
27.900 د. ل	◆ مصاريف نقل من المواني إلى المصنع ( 5 كم )
2.500 د. ل	◆ رسوم إفراج
1.195 د. ل	◆ تأمين بحري
83.648 د. ل	◆ رسوم المطبوعات 8 %

◆ إجمالي المصروفات والرسوم 366.936 د. ل

◆ رسوم ومصروفات = 35 % تقريباً

◆ قيمة الإعتماد 366.936 د. ل

◆ الرسوم والمصروفات 283.288 د. ل

◆ لم تحتسب فوائد المصرف على التسهيلات وهي نسبة 7.5 % 100 وكذلك ضريبة

الإنتاج 10 %

Figure 6.4: The taxes and customs fees on imported raw materials (tins).



The Director of Financial and Administrative Affairs stated that owing to the high volume of taxes and duties the factory should in actual fact be closed and declared bankrupt, as the cost of the production was too high compared with the cost of the imported products in the market; for instance, imported products that receive customs exemption via the economic agreements or through illegal methods of obtaining certain deductions in the duties. Personal relations play a significant role in obtaining certain deductions in the duties. The Director of Financial and Administrative Affairs stated: “I was told by one of my friends that he imported goods to the value of US\$ 20,000 but he used his relatives to reduce this to US\$ 2,000 only for the purposes of customs duty.” Such procedures render illegal competition in the market. Most nationally produced products are selling at a loss (as mentioned earlier) and the price of the competing products will continue to be lower. The solution, from the point of view of the Director of Financial and Administrative Affairs, is to let the foreign investors enjoy the exemptions<sup>26</sup> which the investment law provided for the foreign investor so that the factories could be brought to life once again (the Director of Financial and Administrative Affairs).

The researcher met one of the managers of a privatised factory in the Ministry of Industry in Tripoli Municipality; he stated that the taxation system was far better when the factories were under the public sector and that ‘they are lamenting the old days’. The manager continued:

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<sup>26</sup> Article 10 in the investment Law No.5 of 1997 described these exemptions as follows: A project established within the framework of this law shall enjoy the following benefits:

- 1) an exemption for machinery, tools and Equipment required for execution of the same impact;
- 2) an exemption for equipment, spare parts and primary materials required for the operation of the project, from all custom duties and custom taxes imposed on imports as well as other taxes of the same impact for a period of five years;
- 3) exemption of the project from the income taxes on its activities for a period of five years as from the date of commencement of production or of work, depending on the nature of the project, this period shall be extendable by an additional duration of three year by a decision from the General People’s Committee. Profits of the project will enjoy these exemptions if reinvested. The investor shall be entitled to carry the losses of his project within the years;
- 4) goods directed for export shall be exempted from excise taxes and from the fees and taxes imposed on exports when they are exported;
- 5) the project shall be exempted from the stamp duty tax imposed on commercial documents and bills used.



“When we were under the public sector the production process was strong and the taxation files remained open for several years. There were no serious and immediate claims for paying the taxes because both the factory and the taxation department belonged to the public sector. Now we are forced to pay taxes immediately, otherwise we will face the closure of the factory whatever the situation of our financial or production capacities”.

Table 6.8: A translation of the taxes and customs fees on imported raw materials (pears).

Particulars	Amount
Bank commission	1,488 LD
Bank expenses	943 LD
The Great Man-made River tax 15%	54,111 LD
Custom fees 25%	109,173 LD
Navigation expenses	3,743 LD
Harbor dues	8,060 LD
Transportation fees	4,050 LD
Discharge expenses	<u>505 LD</u>
Total expenses	<u>182,073 LD</u>
Total credit for import	<u>360,746 LD</u>
The percentage of expenses	50%
Production tax	10%
Bank interest	<u>7.5%</u>
Total	67.5%

Source: The accounting statements, Accounting Department, Tripoli, 2001.



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الجمهورية العربية الليبية  
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مصنع الفلام الليبي للمنتجات الغذائية

### إعتماد مركزات كمثري

قيمة الإعتماد : 457.776 فرنك سويسري  
بالدينار الليبي : 360.746 د . ل

❖ عمولة المصرف	1.488 د . ل
❖ مصروفات أخرى للمصرف	. 943 د . ل
❖ النهر الصناعي 15 %	54.111 د . ل
❖ رسوم جمركية 25 %	109.173 د . ل
❖ مصاريف ملاحية	3.743 د . ل
❖ مصروفات مواني	8.060 د . ل
❖ مصروفات نقل	4.050 د . ل
❖ مصروفات تفريغ ومناولة	0.505

❖ إجمالي المصروفات على الإعتماد 182.073 د . ل

❖ المصروفات = 50 % من قيمة الإعتماد تقريباً .

❖ الإعتماد 360.746 د . ل

❖ رسوم ومصروفات 182.073 د . ل

❖ لم تحتسب فوائد المصرف على التسهيلات وهي نسبة 7.5% 100 وكذلك

ضريبة الإنتاج 10 %

Figure 6.5: The taxes and customs fees on imported raw materials (pears).



## **6.8 An assessment of the factory's effectiveness**

It can generally be said that the factory failed to achieve its objectives and targeted plans. This failure is clear since the factory had not achieved the targeted objectives of the production capacity from the very establishment of the factory. Indeed, the production manager argued that the factory has never achieved the targeted production during its life (see section 6.5). Consequently, this underproduction leads to the situation that the factory fails to meet local demand for its product. This failure is a result of many external and internal factors: the shortage of raw materials, spare parts and also state intervention into the factory's activities such as pricing, budgeting and the imposition of high taxes all contributed to this failure. Other visible internal factors are a lack of experience and education among producers/employees in the factory, which prevents the understanding and awareness of the factory's objectives as a means for achieving future plans (see Chapter 9). The central figure in the study is the Secretary of the People's Committee, who has been working in this post at least for 8 years, and manages and controls everything in the factory. All people at different levels in the factory seek his advice before commencing anything, even if it is only a routine process. Hence, the Director of Financial and Administrative Affairs (on behalf of the Secretary of the People's Committee) keeps the maximum amount of personal control over the factory.

To recapitulate, the factory could hardly be described as satisfying its employees, management and (assumed) environment criteria of effectiveness even though it is still working and producing products. Working conditions in the factory were extremely poor, salaries very low and often the latter were delayed because of market conditions and state procedures. Moreover, old technology is still used in the factory and there is a shortage of foreign currency for raw materials and spare parts. These factors and all the above have caused the factory's decline. There were no plans for future investment to improve the efficiency of the factory. Historically, the factory had a good reputation for



providing food products to hospitals and charities but this reputation had gone in view of low sales, and poor trading performance.

## **6.9 Summary**

Management control functions in the factory were both disorganised and irrational. The management of the factory has only a limited role in managing and controlling the factory's activities. The factory's management and structure, accounting system, budgeting system, cost and pricing system and accountability system were discussed in detail in order to gain a rich understanding of the current MCSs in the factory. The Ministry of Industry and the other public agencies still have a vital role in controlling day-to-day processes. Any accounting information produced by the accounting department has little influence on the factory policies and plans and it appears that the state does not consider accounting statements when making decisions regarding the factory's affairs. Indeed, the budgeting system and the pricing system are both controlled by the Ministry of Industry and the Ministry of Economy, hence the government has a vital role in shaping the control function in this factory.



## **Chapter 7: Case No. 2**

### **A Discussion of the MCSs in Al Nur Factory**

#### **7.0 Introduction**

The main aim of this chapter is to describe and discuss the MCSs in the Al Nur Factory (hereafter, ANF). In order to achieve the above aim, this chapter contains a description of the following: an overview of the factory's history; the concept of privatisation and the factory's objectives; the accounting information system; the budgeting system; the cost and pricing system; the reward and accountability systems; an assessment of the factory's effectiveness; and finally a summary of the chapter.

#### **7.1 An overview of the factory's history**

The ANF is a company for the production of paper notepads and was established in 1969 over an area of 4,000 square metres with a production capacity of 10 million paper notepads (of varying sizes) per year. The total number of employees at the time of the company's establishment was 40. On September 1<sup>st</sup> 1989, the ownership of the factory was transferred to the employees and the factory was then further developed to cover 8,000 square metres and the number of producers (employees) rose to 130, of whom 110 were capital holders. The other twenty producers were employed on a contract basis. This salary contract basis contradicted the main principle of the Libyan privatisation experiment, which insists that Libyan citizens must be shareholders instead of salary-paid employees. In terms of the ownership, the different status among people in the factory had reduced the motivation to improve production conditions (see Chapter 9). The capital amounted to 506,000 LD and was distributed equally between these 110 employees, to be paid back to the government at the end of a three-year period. Several production units were added to the factory and the production capacity of the factory increased to 86 million paper notepads per year. This production capacity was sufficient



to cover the domestic demand of the country for paper notepads and paper products with some surplus for export.

## **7.2 The concept of privatisation and the factory objectives**

The privatisation of the factory was projected to have many benefits, as stated by the Secretary of the People's Committee of the factory:

“All the producers now have equal shares in the capital and hence every shareholder has the right to participate in decision-making in the factory. The producer is now the owner of the factory. He is no longer a monthly paid employee. He is no longer achieving profits for others. He is accomplishing profits for him/herself and his/her family”.

Through privatisation, many objectives were realised by paying incentives to the producers to increase production. Now the producers were aware of their responsibility to the factory because they were equal in their duties and rewards, and all were equally responsible for its success or failure. However, from observations at the research site, it is worth noting that the producers' understanding of the privatisation objectives was not equivalent to the state's understanding of these objectives. This is because the application of the privatisation concept was not preceded by any study or planning or even preparation of those concerned for such drastic changes so that they could shoulder their responsibilities. The Secretary of the People's Committee agreed with this researcher's observations by saying that “the producers' awareness of the objectives and targets of the privatisation was very poor. They forget that they are shareholders and claim for payment of their salaries as if the factory is my own property and they are my labourers.” The Head of the Accounting Department said that the privatisation in itself was a good practice, but in reality the principle on which it was applied was that “they dismissed those who were experienced and replaced them with those who were relatives.” Thus, personal relations played a significant role and some people who were not experienced came to hold certain major posts and became decision-makers in the factory. This is why there were no effective planning or control processes, people who held senior posts had no qualifications for these posts and had used their family relationship to get these posts. Therefore, in the case of Libya, the process of the



privatisation was not correctly applied. The following principles for filling these posts were not followed:

1. preparation of reliable well trained people who can understand the objectives of the privatisation and
2. introduction of the concept of the privatisation process in the educational process to produce cadres who have a sufficient knowledge base to apply this concept (according to The Head of the Accounting Department).

One of the accountants mentioned that the concept of privatisation meant that all producers were shareholders in the factory, but planning and administration affairs should be left to personnel who were qualified and well experienced to do the job. The rationale for the idea was not clear to all the producers. Furthermore, every producer wanted to be a member in the factory's management because he saw himself as the owner of the factory. Nevertheless, the Director of Financial and Administrative Affairs argued that the privatisation process had achieved many objectives. First, those who were hired labourers in the past and who did not own any assets in the factory now had shares in the factory. They were also aware of the fact that the more effort they exerted in the factory, the more they would get in return. Indeed, after the initial application of the privatisation concept, the factory achieved quite considerable progress for several years. This was also emphasised by the production manager, who said that the producers previously (before privatisation) had tried to waste time and did not seem interested in increasing production. After privatisation, they started to understand the benefits of working hard, benefits that would be reflected in their standards of living both materially and morally. The production manager stated that the concept of privatisation was a very good idea from a theoretical point of view, but since it was a new idea to be applied for the first time in Libya, the acceptance by the Libyans of this idea was only very limited.

In terms of the factory objectives, the short-term and the long-term objectives were to produce all sizes of paper notepads and all other paper products to meet the local demand. These products are considered essential for all in Libyan society, and the



surplus production is an important export (according to The Secretary of the People's Committee). The Director of Financial and Administrative Affairs argued that the present target of the factory was to cover the local demand of paper notepads for schools. Paper notepads are necessary for all sectors of society and have as inelastic a demand as food and clothes. The long-term objectives will be to produce sufficient notepads to cover local demand and export to foreign markets, i.e. entering the competition in the external markets. There are many hurdles that have to be overcome, such as the availability of ready cash, taxation, funds for replacement and development, and the high exchange rate of foreign currencies.

### **7.3 The factory's management and structure**

The management of ANF has an officially-imposed structure and can be described as follows:

- The factory is managed and controlled by a People's Committee and Congress Committee. Each is composed of five members elected by the Productive Congress and endorsed by the Ministry of Industry in the Tripoli municipality (see Figure 7.1).
- The term of office for the People's Committee members in the factory is five years. The membership can be terminated by the Productive Congress in the case of the following:
  1. loss of credibility and trust as a result of a resolution by the Congress Committee and endorsement of this decision by the Ministry of Industry in the Municipality;
  2. determination of legal judgement that leads to a criminal conviction or a dishonourable offence conviction;
  3. the acceptance of resignation, in the case of death or the end of the term of office.
- The People's Committee may delegate some of its duties to one or more of its members provided that it clearly states in the delegation resolution the limits of



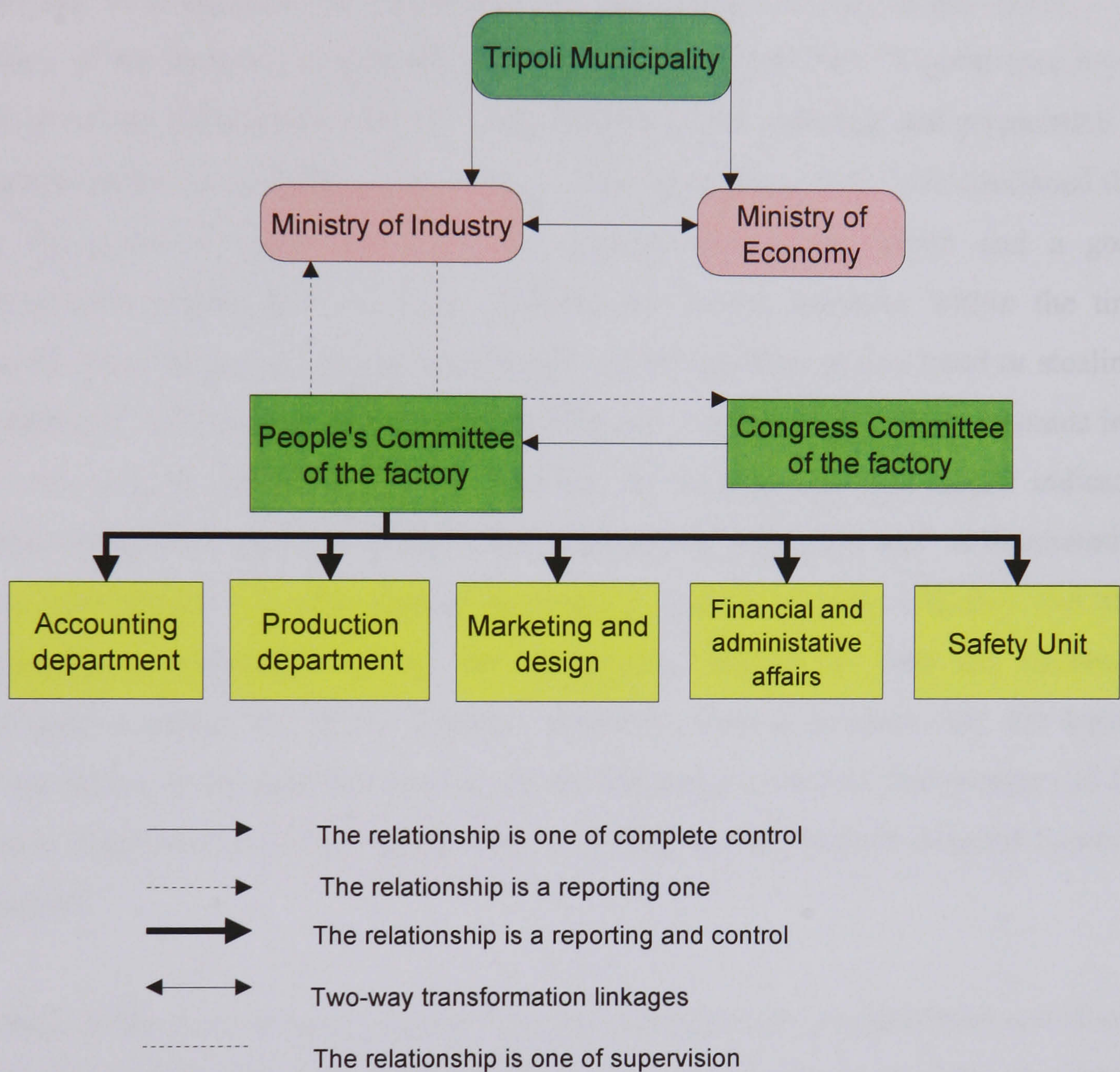
the delegation. The duties of the People's Committee of the factory are as follows:

1. setting up of plans and programmes for achieving the aims of the factory;
2. execution of the resolutions of the Congress Committee for the factory;
3. preparation of the budget projection, the general budget and the final accounts;
4. following up the activities of all factory units in order to guarantee synchronicity of plans and programmes;
5. taking the necessary steps to provide for the factory production requirements at appropriate times;
6. following up factory marketing programmes;
7. issuing internal regulations according to the directives issued for this purpose;
8. Taking any steps necessary for the maintenance of the factory;
9. setting up training programmes in the factory;
10. drawing up proposals for factory development.

The factory shall form a Productive Congress from all members and a People's Committee composed of five members to be selected by direct election. The combining of the role of membership in the Congress Committee and the People's Committee is not allowed. The term of office in the People's Committee is limited to 5 years. The duties of the Productive Congress are as follows:

1. setting the factory's internal policies and the execution of state policies;
2. selection and accountability of the People's Committee of the factory;
3. productive Congress resolutions to be endorsed by the Ministry of Industry in the Municipality;
4. endorsement of the budget and the final accounts;
5. determination of the budget proposal for the coming year;
6. any decision to expel a member or accept a new one.





**Figure 7.1: The structure and the communication and control linkages in ANF.**



## **7.4 The role of the accounting system**

In replying to a question on the role of the accounting system in his factory, the Secretary of the People's Committee of the factory reported that "A good accounting system provides information and data, which helps in the planning and preparation of final accounts for all activities in the factory at the appropriate time." He continued that (from his point of view) the ANF has a good accounting system and a good documentation system and the final accounts are always prepared within the time requested. This, he argued, is a good indication of the absence of any fraud or stealing. He continued: "It is known that factories, which fail to prepare their final accounts in a good time will be criticised by those owning the factories, as this failure indicates financial difficulties such as fraud." The Director of Financial and Administrative Affairs also argued that the applied accounting system is very effective and that management is supplied with all the information needed to take the necessary administrative actions for all the factory's activities, such as product cost. He argued that "our factory is the only one that has sound and proper accounts, and prepares all the necessary final accounts at the proper time and there are no debts or external financial obligations".

The Head of the Accounting Department argued that the lack of specialised and skilled personnel in the accounting department resulted in poor development of the accounting system. He reported that before privatisation people in the factory used a very primitive system of accounting, depending only on invoices, cash records, and a double register of debtors and creditors. At the end of every year they compared the two sets of figures to arrive at a result. He pointed out that now, after privatisation, the factory keeps registers and main accounts for all activities, such as the general journal in which all transactions and deals are registered and the final accounts and the estimated budgets are prepared. Yet, he suggested that "None of these accounts are in fact used because nobody really understands how they can be useful in planning, controlling and improving performance".



With regard to the books and records in the factory, all books and records specified by the Libyan Commercial Code (LCC) should be kept. These are as follows:

1. the general journal in which all financial transactions of the factory must be recorded;
2. bank ledgers in which all banking transactions are registered;
3. cash ledgers in which all cash transactions are registered;
4. a general ledger in which separate accounts are opened for every item to show each year's status and balance.

From the researcher's quite lengthy stay in the factory, especially in the accounting department, it was observed that the role of the accountant was just to put together the accounts of the factory rather than explicitly to prepare information useful for management. The accountant did produce *ad hoc* reports as the management requested. These requested tended to be of a quite limited nature; e.g. for a report of the year profit, such a request might be satisfied by simply handing over the accounts. On many occasions, the accountant orally reported on the profits or expenses of the factory. While accounting information is used frequently in decision-making today with regard to such matters as product costing and pricing (Kaplan and Atkinson, 1998; Drury, 1996), nonetheless the role of accounting in respect of such considerations remains very limited at ANF. The Head of the Accounting Department described the financial control dimension as being very weak. He illustrated this by referring to the documentary cycle in the factory as like 'an inverted pyramid'. From his point of view, the documentary cycle of purchases, for instance, should pass through the following steps. An application, detailing the required quantity of materials should be sent to the stores, and if these things are unavailable in the stores the storekeeper should request the purchase of them. This purchase order should then be sent to the accountant for an estimate of the price and place of purchasing. According to the accountant's estimation, funds should be paid to the purchase agent to purchase the required materials. Once purchases are made, the goods should be stored in the factory and categorised, and all the purchase documents referred to the accounting department for registration and comparison.



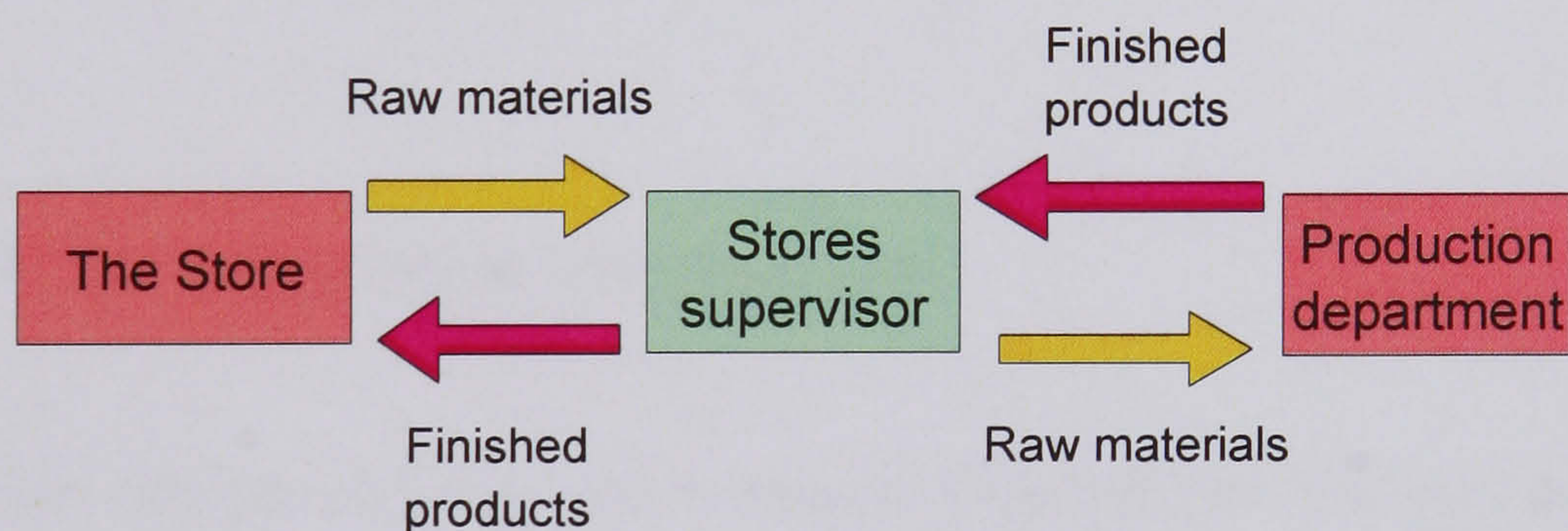
In practice, for the Head of the Accounting Department, this is not what happens. Instead, if materials are not available in the store, the store-keeper makes the order to purchase verbally through the purchase agent who will then purchase the material at a price without the immediate scrutiny of the accountant. The invoice is later referred to the accounting department for settlement only. There is no fixed policy or procedure for evaluating the stocks in the stores, nor any plan of stock re-ordering point or storage safety. The weak documentary cycle is clear in the case of the system of subsidies granted by ANF for participation in the social and national festivals. The most appropriate method for the Head of the Accounting Department is that the Festival Committee should make proposals for the kind and cost of the participation and present these to the finance section to see whether the financial capability of the factory permits such expenses. So, the decision of the Committee should be based on the recommendations of the finance section. However, in practice, this is not the case, as the Festival Committee does not usually pay any attention to such directions. According to the Head of the Accounting Department, they execute the programme at a very high cost without any reference to the finance section, and they send their invoices for payment after the end of the festival.

Another point is that, as a result of the lack of specialised and skilled accountants, there is no separate cost accounting section in the factory and the general accountant of the factory is responsible for the preparation of the cost accounts. The product cost statement is discussed with the management before being sent to the Ministry of Economy, in the context of getting approval of the sale price (see section 7.6 on the pricing system). The Head of the Accounting Department stated that proposals by himself for changes and additions to the accounting system were sometimes presented with a view to improving it and to achieving targeted objectives. Unfortunately, he reported that all these proposed changes did not amount to very much development in practice because of a lack of specialised and skilled personnel, a lack of awareness of the procedures to attain objectives and a lack of awareness of the status and general benefits of such changes. The Head of the Accounting Department argued that “Producers do not understand the objectives of the privatisation nor do they take



responsibility for the factories because they did not pay to own the factory.” One of the proposals to develop accounting in the factory sought to establish and operate a model system for the control of stocks in the stores and movements of stocks from stores to production. This was intended to control the outgoing raw materials to the production department and the in-coming finished products to the store, a process that needs to be conducted with specific standard specifications to minimise loss. Figure 7.1 shows the previous situation of the relationship between stock and production. The production department could ask for the materials from stores verbally. It appears that there is no kind of control or supervision of the stores supervisor who receives the raw materials and delivers the finished products, a lack of control that encourages people to exploit the system for their own ends.

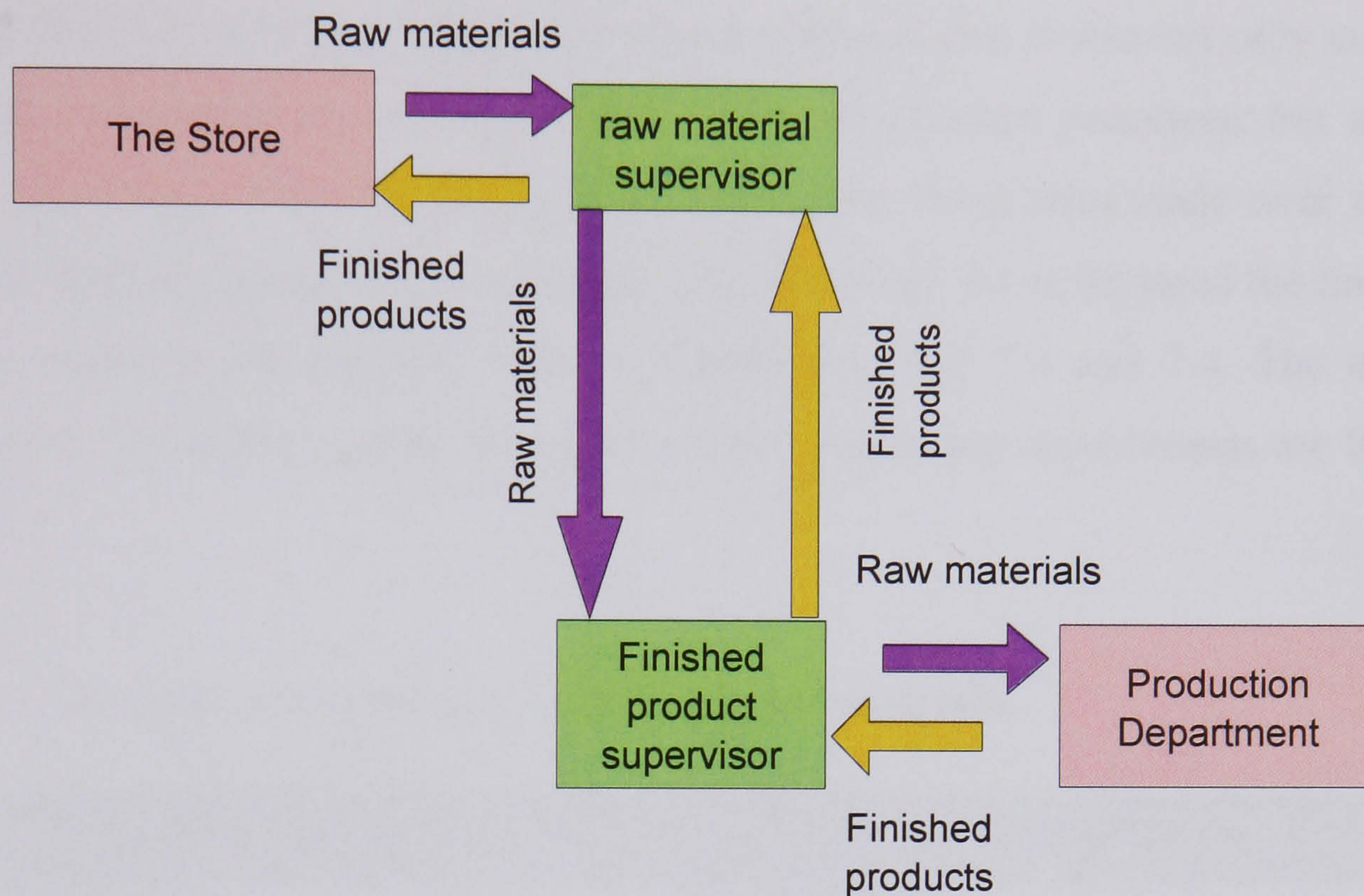
**Figure 7.2: The current production cycle.**



The alternative system proposed by the Head of Accounting Department consists of two people instead of one. The first one is the raw material supervisor while the other one is the finished product supervisor. The raw material supervisor receives the raw materials (RM) and delivers them to finished products supervisor who in turn delivers finished products to the raw materials supervisor who returns it to the store. Both should prepare reports of the received finished products and raw materials, and by doing so, the management can say that they have separated the cycle. From these two reports, people in charge can determine the quantity of finished products and the level of raw materials available in stock. Consequently, the management could determine the reordering point



for raw materials and the quantity of surplus raw materials during the production process. For further control, the raw material supervisor should come under the control of the store administration while the production supervisor should come under the control of the financial administration (see Figure 7.2).



**Figure 7.3: The suggested production cycle.**

Unfortunately the person who was entrusted with this job (finished product supervisor) left the factory, and the factory returned to the previous system owing to a lack of trained personnel to carry out such a job.

The second proposed change involved the operation of a gate book, requiring an administrator with significant accounting experience. The proposed book had two parts, one for incoming items (coming into the factory) and the other for out-going items. In each case a register was to show a gate book number, driver name, type of material, quantity, invoice number and time and date. This is very important for comparing materials as these pass through the gate, with those received by the store-keeper and the accountants' records. The out-going items should be compared with those entering the gate. As an example the accountant can compare the sales and purchases invoices with



the quantities in the gate book to control these processes. Unfortunately, this was practised for only a limited time, owing to a lack of skilled personnel able to perform such jobs, and a lack of a sense of responsibility and awareness (according to the Head of Accounting Department).

The Head of the Accounting Department also mentioned that it was not only unskilled people that were hindering the development of more efficient processes, but also the high tax rates imposed by the state, taxes such as the Great man-made river tax, the custom tax and the change in the exchange rate of the LD. To understand the impact of the above taxes on the product cost, see Tables 7.1, 7.2, 7.3 and 7.4. The targeted production is 12.6 million paper notepads and the production requirements are listed in Table 7.1:

Table 7.1: The costs of producing 12.6 million paper notepads.

Particulars	Amount
White paper 60 gm	1,700 Ton
Cover 180 gm	163,800 Ton
Carton	105,000 carton
Administrative expenses	463.613 LD per Ton
Delivery expenses	0.500 LD per Ton
Transferred fees	12 LD per Ton
The great man-made river tax	15% from raw materials invoice
Custom duty	12.5% from raw materials invoice
The cost of the white paper	870 LD per Ton
The cost of the cover	2,260 LD per Ton
The cost of the carton	0.55 LD per carton

Source: The production reports, Tripoli, 2002.



Table 7.2: Cost of the producing the paper notepad in respect of the white paper and the notepad cover in Libyan currency at an exchange rate of 0.65 LD against 1 US\$.

Particulars	Cost 1 (a)	Cost 2 (b)	Cost 3 (c)	Cost 4 (d)
<b>White paper:</b>				
Original price	961,350	961,350	961,350	961,350
Great man-made river tax 15%	144,202.500	If not paid	144,202.500	If not paid
Custom tax 12%	120,186.750	If not paid	If not paid	120,186.750
Transportation expenses	20,400	20,400	20,400	20,400
Delivery fees	850	850	850	850
Total	1,246,971.250	982,600	1,126,802.500	1,102,768.750
Cost of one Ton	733.513	578	662.825	648.688
Cost of one pad	99 Derham	78 Derham	89 Derham	88 Derham
<b>The cover :</b>				
Original price	2,406,622.200	2,406,622.200	2,406,622.200	2,406,622.200
Great man-made river tax 15%	36,093.330	If not paid	36093.330	If not paid
Custom tax 3%	7,218.666	If not paid	If not paid	7,218.666
Transfer expenses	1,965.600	1,965.600	1,965.600	1,965.600
Delivered fees	81.9	81.9	81.9	81.9
Total	285,981.696	242,709.700	278,803.030	249,928.366
Cost of one Ton	1,745.920	1,481.744	1,702.094	1,525.814
Cost of one pad	230 Derham	190 Derham	220 Derham	200 Derham

Source: The accounting statements, Accounting Department, Tripoli, 2002.

- (a) This assumes that the Great man-made river tax and the custom tax are paid.
- (b) This assumes that the Great man-made river tax and the custom tax are not paid.
- (c) This assumes that the Great man-made river tax is paid, but the custom tax is not paid.
- (d) This assumes that the Great man-made river tax is not paid, but the custom tax is paid.



Table 7.3: Cost of the producing the paper notepad in respect of the white paper and the notepad cover in Libyan currency at an exchange rate of 1.210 LD against 1 US\$.

Particulars	Cost 1	Cost 2	Cost 3	Cost 4
<b>White Paper:</b>				
Original price	1,789,590	1,789,590	1,789,590	1,789,590
Great Man-made River tax 15%	268,438.500	If not paid	268,438.500	If not paid
Custom tax 12.5%	223,698.750	If not paid	If not paid	223,698.750
Transfer expenses	20,400	20,400	20,400	20,400
Delivered fees	850	850	850	850
Total	2,302,977.250	1,810,840	2,079,278.500	2,035,538.750
Cost of one Ton	1,354.693	1,065.200	1,223.105	1,196.788
Cost of one pad	183 Derham	144 Derham	165 Derham	161 Derham
<b>The cover :</b>				
Original price	447,927.480	447,927.480	447,927.480	447,927.480
Great Man-made River tax 15%	67,189.122	If not paid	67,189.122	If not paid
Custom tax 3%	13,437.824	If not paid	If not paid	13,437.824
Transfer expenses	1,965.600	1,965.600	1,965.600	1,965.600
Delivered fees	81,900	81,900	81,900	81,900
Total	530601.926	449,974.980	517,164.102	463,412.804
Cost of one Ton	3,239.328	2,747.100	3,157.290	2,829.138
Cost of one pad	420 Derham	360 Derham	410 Derham	370 Derham

Source: The accounting statements, Accounting Department, Tripoli, 2002.

Table 7.4: The total cost of the paper notepad in Libyan currency at an exchange rate of 0.650 LD against 1 US\$.

Particulars	Cost 1	Cost 2	Cost 3	Cost 4
White paper	1,246,971	282,600	1,126,803	1,102,769
Cover	285,981	242,710	278,803	249,928
Carton	57,750	57,750	57,750	57,750
Administrative expenses	788,141	788,141	788,141	788,141
Total	2,378,843	2,071,201	2,251,497	2,198,588
Loss in materials	118,942	103,560	112,575	109,929
Total	2,497,785	2,174,761	2,364,072	2,308,517
Total cost of one pad	198 Derham	172 Derham	187 Derham	184 Derham

Source: The accounting statements, Accounting Department, Tripoli, 2002.



Table 7.5: The total cost of the paper notepad in Libyan currency at an exchange rate of 1.210 LD against 1 US\$.

Particulars	Cost 1	Cost 2	Cost 3	Cost 4
White paper	2,302,977.250	1,810,840	2,079,278.500	2,034,539
Cover	530,601.926	449,974.980	517,164.102	463,413
Carton	57,750	57,750	57,750	57,750
Administrative expenses	788,141.379	788,141.379	788,141.379	788,141
Total	3,679,470.555	3,106,706.359	3,442,331.981	3,343,842
Loss in materials	183,973.528	155,335.318	172,116. 699	167,192
Total	3,863,444.083	3,262,041.677	3,614,450.680	3,511,035
Total cost of one pad	307 Derham	259 Derham	287 Derham	279 Derham

Source: The accounting statements, Accounting Department, Tripoli, 2002.

In the above Tables costs 1, 2, 3 and 4 represent the product cost assuming the paying or not paying of the imposed taxes. Cost 1 shows the impact of paying all the taxes on the product cost (notepads), and cost 2 highlights the product cost if the factory does not pay the taxes. Costs 3 and 4 respectively show the product cost if the custom tax and the Great Man-made river tax are not paid (see Tables 7.2 and 7.3).

### 7.5 Budgeting system

In terms of budgets, the Secretary of the People’s Committee stated that there was no reason for preparing and making budgets, since they were never given any attention in practical application. In fact, according to the Secretary, given the volatility of Libyan market they could not be taken as a basis for comparison against outcomes to ascertain and act upon any anomalies. There were no parameters for planning or projecting future work and the presence of so many government imposed handicaps and restrictions such as the limitation on import budgets and foreign currency, the fluctuation of exchange rates and the imposition taxes and ever-increasing fees, prevents effective planning and control. This is why it was impossible to make a future plan for any activity (according



to the Secretary of the People's Committee). Nevertheless, some operational budgets were prepared to show the raw materials and spare parts needed for the production process, and these budgets were presented to the Ministry of Industry, along with production reports to satisfy the requirement to approve imports. Imported raw materials usually come in small quantities, far below the actual needs of the factory. Consequently, on many occasions the factory has been closed owing to a lack of raw materials (the Secretary of the People's Committee) (see Table 7.6 and discussion below). From this researcher's discussion with members of the People's Committee it can be concluded that the operational budgets are in fact prepared merely to fulfil the required conditions.

From Table 7.6 the negative effect of the cessation of state foreign currency support on the production capacity can clearly be seen. In 2000 and 2001 the targeted production was 100% of the designed capacity but in 2002 the targeted production was reduced to just 32%. People in charge at the Ministry of Industry do not evaluate the operational budgets. They actually ask the factory's management to prepare a budget but this appears to be ignored in policy decisions. The Secretary of the People's Committee highlighted this situation by saying that:

“On the one hand the Ministry of Industry asks for the preparing and sending in of these operational budgets at the right time, while on the other hand they do not shoulder any responsibility for solving the problems faced by privatised factories. They (the people in the Ministry of Industry) say these factories are now privately owned and the producers should bear their responsibilities and solve their problems”.



Table 7.6: The operational budgets of 2000, 2001 and 2002.

Particulars	Amount (LD)	Targeted production	Optimum capacity	%
Raw materials	16,841,024.020			
Spare parts	858,783.663			
Help materials	224,030.523			
Asset development	1,859,550			
Asset replacement	531,300			
Transportation	101,200			
Total operational budget	20,415,888.206 (1)	84,538,000 notepads (2)	84,538,000 notepads (3)	100% (2/3)
The allocation of the factory from the import budget 2000	1,530,000 (4)			8% of required need (4/1)

Particulars	Amount (LD)	Targeted production	Optimum capacity	%
Raw materials	16,841,024.020			
Spare parts	858,783.663			
Help materials	224,030.523			
Asset development	1,859,550			
Asset replacement	531,300			
Transportation	101,200			
Total operational budget	20,415,888.206 (1)	84,538,000 notepads (2)	84,538,000 notepads (3)	100% (2/3)
The factory's allocation from the import budget 2001	US\$ 700,000 around (1,050,000 LD) (4)			5% of required need (4/1)

Particulars	Amount (LD)	Targeted production	Optimum capacity	%
Raw materials	6,070,156.745			
Spare parts	235,865			
Help materials	61,530			
Asset development	1,859,550			
Asset replacement	531,300			
Transportation	101,200			
Total operational budget	8,859,601.745 (1)	27,000,000 notepads (2)	85,000,000 notepads (3)	32% (2/3)
The allocation of the factory from the import budget 2002	Zero (4)			0% (4/1) of required need.

Source: The production report, Tripoli, 2000, 2001 and 2002.



تقرير تطور الانتاج الصناعي  
 بمصنع الور للكرسات والمبجات الورقية  
 خلال الفترة من : 1 / 1 / 1402  
 الى : 31 / 12 / 1402  
 3- المراجعة النهائية

اسم المصرف المعامل معه :

رصيد المواقفات		الاعتمادات المتوقعة خلال الفترة								قيمة المواقفات	قيمة المراجعة المعتمدة	
اعتمادات لدى	اعتمادات لدى المصرف	الاجمالي	قيمة الالات	قيمة مستلزمات	قيمة قطع غيار	قيمة مواد خام	اسم البلد المورد	تاريخ الاعتماد	رقم الاعتماد	الصادرة ( دينار )	( دينار )	
		698500				698500	البحرين			700000	700000	
		دولار				دولار				دولار	دولار	



امضاء مدير عام  
 2002  
 1/9

Figure 7.4: The foreign currency allocation for year 2001.



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وصف المرافقات

الاعتمادات المفتوحة خلال الفترة

قيمة المرافقات  
الصادرة ( دينار )

قيمة المراجعة المتعددة  
(دينار)

التشاركية	المؤسسات
المؤسسات	المؤسسات

652

وَمَا يَكْفُرُ

ج  
مستخرجات

فیه قطع  
خار

قیمۃ مواد  
خام

اسم الطائر  
المرور

الشيخ الاسلام

رقم الاعتماد

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The Head of the Accounting Department mentioned that the operational budgets are prepared every year, but that under the prevailing conditions it was very difficult to make one proposal for the budgets as the market was unstable, making forecasts and estimates very difficult. Nevertheless, each year the accountants try to determine the variance from the norm<sup>27</sup>, whether positive or negative. In most cases the variance is negative, and this is mostly as a result of the changes in the environment impacting upon the costs of business. Negative variances are treated by creating a marked positive variance in other items, i.e. if the item of the equipment maintenance was 15,000 LD and the estimated figure was 10,000 LD then the negative variance would be 5,000 LD. In the following year the maintenance item would be estimated at 15,000 LD, and a reduction would be made in another positive item, such as the remuneration item or the incentive items, by 5,000 LD (The Head of the Accounting Department).

Despite all the effort that goes into the preparation of the budgets they are still not used from an administrative or control point of view and are prepared only as a routine to satisfy the authorities in the Ministry of Industry. One of the accountants argued that:

“The fact that the budgets are not used is owing to two reasons. First, it was very clear that in the period before the flotation of the Libyan Dinar against the U.S dollar, the Ministry of Industry was controlling the import budgets and we got very little funds, which were not sufficient to cover our import needs and achieve our targets. Second, as a result of this change in the exchange rate, the factory started to face a lack of cash to import the inputs starting in 2003, when the U.S dollar became equivalent to 1.5 LD, instead of 0.300 LD. In the meantime there is no good banking system able to extend loans. Consequently, the budgets lose their use and value.”

The Production Manager supported the idea that the import budgets and the allocation of foreign funds represented the most important factors restricting the production process. The targeted production was 86 million paper notepads per year, but the allocated funds could be enough for only 10% of this quantity (about 10 million paper notepads or 10-11 % of the targeted production). The factory's production could hardly cover its fixed expenses (the Production Manager). Yet the factory has no option but to



accept these procedures because there is no other way to secure foreign currency except from the Ministry of Industry. If the factory resorts to locating other sources for foreign currency it will face criticism and legal enquiries. This kind of procedure encourages the accountants and the management of the factory to actually manipulate the figures in the import budgets in order to obtain sufficient allocation of foreign currency, and if they get more than they need (this is unlikely to happen according to the evidence collected) they could re-allocate it to other areas. As a result of government intervention in the budgeting process, most of the factories' budgets are inaccurate (the Director of Financial and Administrative Affairs).

#### **7.5.1 The budget committee**

The budget committee is composed of four parties representing each of the following departments: maintenance, technical, financial and production. All items of the budget are discussed by this committee and several meetings for discussion take place between the financial department and the production department. The production department usually wants the best quality of product, irrespective of the cost, whereas the financial department places a priority on cost and the best price for the market. The production and technical departments then suggest the specifications, while the financial department suggests the cost, and the final decision rests within the financial department, since it is the body that can decide on the available cash and budget of the factory. After discussion of the budget with the factory's management, the budget is referred to the Ministry of Industry where the share of the factory from the import budget is determined, which usually falls short of the actual needs of the factory.

### **7.6 Cost and pricing system**

The Ministry of Economy is the authority that fixes the sales prices of the paper notepads and all other paper products. The paper notepads are considered absolutely essential products that everybody uses. Therefore the Ministry of Economy at the national level very frequently fixes the prices of paper notepads in the same way as with

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<sup>27</sup> This does not imply that standard costing was in operation. The variance was only from the value stated



any other strategic commodity. The Secretary of the People's Committee argued that the paper notepads are in fact equal in importance to food products. As a result of this view, the state prices of paper products are not based on product cost. Accordingly, very often the prices fixed for paper notepads are below the cost of production (see Table 7.9 and 7.10 for cost calculation). The accounting department used to prepare a costing schedule for these paper notepads and send it to the Ministry of Economy in the Tripoli Municipality to help in fixing the final sale price (Table 7.9 and 7.10). The Head of the Accounting Department suggested that "The Ministry of Economy should be well equipped with all the necessary information and data bases and cost calculations since it is the authority responsible for fixing the sale prices of all products in the country. Yet unfortunately, the Ministry of Economy depends on the information provided by the factories, which may not be sound or may be vague and deceptive." The Director of Financial and Administrative Affairs concluded that:

"The Ministry of Economy has no specialised cadres for providing such information as costing and commodity prices. It has no information system. They frequently used to make unfair decisions based on personal judgements".

One of the accountants said that:

"[O]ne person in the Ministry of Economics in Tripoli Municipality, because of ignorance or a lack of experience, or for some personal reasons, may damage the future prospects of around 130 families in the factory by making wrong decisions regarding the prices of the products".

It is very common in the paper industry for the government to intervene in the pricing policies in order to control products. On many occasions the government determines the sale price of paper products without any prior consideration of the products' cost or the flexibility of the demand for these products (see Table 7.11). Table 7.11 shows government decision No. 318 regarding the final sale price of the paper notepads in the country.

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in previous budgets.



Table 7.7: Al-Nur factory price for producing 12.6 million paper notepads at exchange rate of 1.210 LD against 1US\$.

Particulars	The amount (LD)	US\$
Total cost of the paper notepads*	3,863,444.083	3,192,929
Price combined 3%	115,903.322	95,787.869
Pricing fees 2.5%	9,948.369	8,221.793
Total	3,989,295.774	3,296,938.662
Sales tax 3.5%	139,625.352	115,392.853
Total sales price	4,128,921.126	3,412,331.505
The sales price of one paper pad	0.328 LD or 328 Derham**	0.271

\*See section 7.4 for the calculation of this figure.

\*\* One LD = 1000 Derham

Source: The accounting statements, Accounting Department, Tripoli, 2002.

Table 7.8: Proposed price of 10 million paper notepads at an exchange rate of 1.5 LD against 1 US\$.

Name	The amount LD	US\$
White paper 80gm	1,971,606.368 LD	1,314,404.245
Coloured cover 180gm	516,114.315 LD	344,076.210
Packing boxes	56,100 LD	37,400
Administrative expenses	789,966.735 LD	526,644.49
Total	3,333,797.418 LD	2,222,524.945
Margin 5%	166,689.871 LD	111,126.247
Combining prices 3%	100,013.923 LD	66,675.748
Pricing fees 2.5%	83,344.935 LD	55,563.124
Sales tax 3.5%	116,682.910 LD	77,788.373
The sale price from the factory	3,633,839.186 LD	2,533,678.437
The sale price of one paper notepad	363 Derham	0.253

Source: The accounting statements, Accounting Department, Tripoli, 2002.



Table 7.9: The sale prices for paper notepads in the whole country.

Particulars	Size (cm)	Factory's sale price to state	Factory's sale price to shops	Final customer's sale price
40 page school pad	21* 16	0.135 LD	0.150 LD	0.160 LD
60 page school pad	21 *16	0.185 LD	0.205 LD	0.220 LD
80 page school pad	21 *16	0.240 LD	0.270 LD	0.290 LD
80 page university pad	21* 28	0.765 LD	0.855 LD	0.900 LD
60 page note pad	21* 16	0.200 LD	0.220 LD	0.230 LD
100 page university pad	21* 28	0.640 LD	0.710 LD	0.750 LD

Source: The state decisions, Ministry of Economy, 2000.

From Tables 7.7, 7.8 and 7.9 it is apparent that the cost of an 80-page school notepad is 0.328 LD whereas the sale price from the factory to government is only 0.240 LD. And, even the sales price to the final customer is less than the factory's cost of 0.306. Implementing this official decision means that the factory is selling its products at a loss. The Head of the Accounting Department argued that “decisions like that push the factory to make huge losses because of low selling prices compared with the production cost, and if the government does not rethink the selling prices the factory will continue to make losses.”

### 7.7 The reward, penalty and accountability systems

Prior to privatisation all labour disputes had been settled by state arbitration. Since privatisation this mechanism has been removed and labour problems have become almost impossible to resolve due to the lack of organisational procedures for this purpose. For example, since there are no regulations or bylaws to stipulate the rewards and penalties in the privatisation process, the management of the factory is unable to enforce penalties or pay rewards to the producers (employees). The Secretary of the People's Committee argued that “It is impossible to suspend or fine any producer or even deduct a certain amount of money from the producer for instance, in the case of



absence.” The Secretary mentioned a certain case where a producer was absent from work for about 20 days and the secretary issued an order suspending him from work. The producer then raised a case in the nearest court and the court issued an order in his favour because there are no such bylaws or regulations to give the Secretary the right to issue such a penalty. The producer subsequently returned to his job without any penalty. This case deeply affected the morale of the other producers who were committed to their work. There was no longer any incentive for work, so absenteeism amongst producers increased greatly. Indeed, some producers even started to take pleasure in being absent (the Secretary of the People’s Committee).

Thus, this absence of internal by-laws regulating work and determining rights and liabilities or rewards and penalties poses great problems to producers who do not comprehend the concept of privatisation because of their lack of education and experience. This is negatively affecting the progress of the production process. The Head of the Accounting Department said that the heads of departments in the factory had no right to implement penalties or any other procedures on the producers. He argued that:

“[T]he production manager, for example, cannot ask the producers to work overtime. Sometimes the producers may ask the manager to share the work on the grounds that he has as equal a share as they have in the capital of the factory and therefore they should also be equal in their duties”.

The Director of Financial and Administrative Affairs mentioned that there were no penalties or rewards because, as producers assert, all are equal as producers. He continued that:

“As a person in charge I could not rectify the situation directly. I can only suggest proposals for solutions and show the defects and the way to cure them. The producers have the option to correct the defects or leave them when they discuss these issues in their Productive Congress”.

The Productive Congress is the highest controlling authority in the factory to control and call into account the People’s Committee regarding its performance and its achievement of the factory’s objectives and plans in both the short and long run. In



terms of accountability periodical meetings are held at the factory level to discuss problems when they arise. This discussion also includes the achievement of plans drawn up by the Productive Congress for the People's Committee to execute the targets of the factory. However, from the investigation of the available records it was found that no such meetings had been held for two years, which means the control function in the factory was lost. Indeed, the Secretary of the People's Committee noted that "The Secretary of the Congresses Committee has no practical role except on paper, because he receives many personal facilities (loans, cars etc.) so these benefits hinder his ability to criticise the People's Committee. In this way, we (the management) avoid the problems of changing the members of the People's Committee."

From reading the reports and the minutes of the meetings it was indeed clear that the Secretary of the People's Committee had not changed since 1990. Also, when interviewing the members of the Congress Committee they acknowledged that they considered themselves weaker than the members of the People's Committee. Producers had raised their problems with the People's Committee for solutions if the problem was connected to production. If the producers' problem or complaint was about the People's Committee the claim was raised with the Congress Committee. The People's Committee was held responsible to find a solution for their problem, yet contrary to the official rules and procedures, the effectiveness of a claim raised by the producers to the Congress Committee was very weak (as stated by the Secretary of the People's Committee). In fact, the Secretary of the Congress Committee took his personal problems to the Secretary of the People's Committee to solve them financially or personally.

From the above it can be concluded that a lack of awareness and understanding of the rights and obligations, and also the unclear nature of the relationship between the People's Committee and the Congress Committee both pose serious problems to the effective running of the factory. The Production Manager stated that there were no accountability meetings between the factory and any external parties.



## **7.8 Salaries, wages and the factory development functions**

Since the capital of the privatised factories is divided into shares with equal values, each producer has the right to have a certain number of shares and each producer has an equal share of the capital. The general principle in the privatised factories is to distribute the return equally between the producers, since they have equal shares. However, the application of this principle will favour certain producers such as those who joined the factory just before the privatisation date and are now treated equally with producers who have spent their entire working lives in the factory. The Secretary of the People's Committee argued that if the shares from the returns were equal there would be no incentive for production nor any bearing of responsibility. This is why the factory's management proposed a system of salaries or monthly drawings that varied according to the qualifications and experience of each producer. To apply this system, certain points were given for attendance, behaviour, seniority, qualifications and experience. These characteristics were listed in the personnel files in order to determine a ranking for each producer. The Head of the Accounting Department argued that:

“It is unfair that those who are more qualified and more experienced receive the same salaries with the others. A person who has been working in the factory for 28 years should not get the same salary as the producer who joined the factory just a few months before the privatisation process was applied for”.

The only solution in this case would be a difference in salaries. At the end of the year all the salaries were deducted from the outcome of the transactions. If there were a profit it would be equally distributed among the producers. This proposal was approved in a general meeting of the Productive Congress, and thus variations in the producers' salaries are planned. The proposal for graded salaries is being implemented in the factory at present (the Head of the Accounting Department).

The development of the privatised factories to attain the targeted production and quality is one of the most important objectives for their management. To realise this objective the Secretary of the People's Committee suggested assistance from three different



sources: 1) the state must support privatised factories by providing funds for development and replacement processes. This solution is far from being realised because the state has avoided carrying the financial burdens of these factories, especially after the flotation of the LD. The Secretary of the People's Committee stated that "we applied to the Ministry of Industry in Tripoli Municipality for a development and replacement fund 15 years ago and not one Libyan Dinar was given." 2) The banks should provide the necessary loans and banking facilities for these factories, yet owing to the lack of a developed banking policy a large number of handicaps and problems have arisen. The loans are not large enough to serve development and replacement needs. Moreover, the banks apply an interest rate as high as 7.5% on these loans. This interest is prohibited in the Islamic religion, therefore this prohibition has a negative impact on the factories' activities (see Chapter 9). 3) The company's own resources: since the only source of income is the revenue from product sales, especially from the sales of paper notepads and booklets for schools, financing the development and replacement plans from this revenue means that no profits will be distributed for many years. This policy (profit capitalisation) needs approval from the Productive Congress of the factory, where all producers can participate. This issue has been presented in the Productive Congress several times but as yet, no solution has been reached, owing to the lack of awareness of the importance of development and replacement among producers. This is why the factory remained without any development for a long time. The Production Manager argued that:

"The producers are unwilling to capitalise the profits because they want the profit to be distributed among them as they are not aware of the benefit of developing the factory and, because they have no trust in the political resolutions of the country. Moreover, the nationalisation of Al-Afia Clinic<sup>28</sup> was one issue that resulted in a lack of faith and trust in the resolutions taken by the state".

One producer commented on this by saying that "it is important to solve today's problems, as far as tomorrow's problems are concerned I leave them for tomorrow." From the field observations it is notable that most shareholders are young people who have typical financial and social commitments (for instance, marriage costs). As a

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<sup>28</sup> Al-Afia clinic was a private clinic. The Government renationalised it and it became a public clinic.



consequence, most of them refuse to capitalise the factory's profits. One of them argued that "Our financial commitments are not liable for any postponement. I should solve today's problems and tomorrow's may not come at all." Another one said that "if we are convinced of the idea of profit capitalisation, and suddenly a decision is issued by the state to cancel the privatisation of the factory or return it to the public sector, in this case we will be the only losers".

## **7.9 Assessment of the factory's effectiveness**

It can be said that the factory succeeded in achieving one of its objectives, that of making an annual profit from its activities and this is because of the high demand for the paper products (see section 7.1). Yet the factory failed to achieve other objectives such as achieving its targeted production. This failure to achieve the targeted objectives of its production capacity has been evident since its establishment. The Production Manager and the Director of Financial and Administrative Affairs argued that the factory has never achieved the production target during its life (see section 7.5). Consequently, this shortage of product quantity led to the situation that the factory failed to meet the local demand for this product and lost the chance of exporting its products. This failure is a result of many external and internal factors. The shortage of raw materials, and spare parts, economic sanctions, and state intervention in the factory's activities such as pricing, budgeting and high taxes have all contributed to this failure. The prominent internal factor is the lack of experience and education among people in the factory, which prevents an understanding and awareness of the factory's objectives as a means for achieving future plans (see Chapter 9). The central figure in the study was the Secretary of the People's Committee who has been working in this post for 13 years and manages and controls everything in the factory. This was in direct contrast to what is stated in written documents such as the ownership contract, which states that the factory is managed and controlled by Committees.

All the above factors have led to the factory's failure to achieve any real success. Furthermore, were there no plans for future investment to improve efficiency. Although the factory has a good reputation in the local market because of the quality of its



products compared with some imported products (e.g. notepads from Egypt), without state support most of the national products will fail before they are even launched (see sections 7.5 and 7.6).

To conclude this section, it may be said that the factory can hardly be described as satisfying its employees, management or (assumed) environmental criteria of effectiveness, even though the factory is still working, producing products and making profits. The working conditions were very poor, the imported raw materials and spare parts were frequently delayed because of either market conditions (sanctions) or state procedures. Moreover, old technology was still being used in the factory and there was a shortage of foreign currency for raw materials and spare parts.

## **7.9 Summary**

This chapter has explored and discussed the actual situation of management control functions in the ANF. The factory's objectives, management and structure, accounting system, budgeting system, cost and pricing system and salaries and reward system were discussed in detail in order to achieve the research goals. It appears that the factory's management has only a minimal influence on its day-to-day activities. Much of the accounting information was not used to manage and control the factory's processes in order to achieve its objectives. After exploring and understanding the impact of the external environment on the control function in the factory, it is concluded that the public agencies, economic sanctions and social relations play a dominant role in managing and controlling the factory. Budgeting, pricing and election processes are in effect controlled by the Ministry of Industry or the Ministry of Economy, even though, under privatisation, these things were supposed to be managed and controlled by the factory.



## **Chapter 8: Case No. 3**

### **A Discussion of the MCSs in The Brick Factory**

#### **8.0 Introduction**

This third case study was conducted in ‘The Brick Factory’ (hereafter, TBF). This chapter describes and discusses the current MCSs in TBF and contains a description of the following: an overview of the factory’s history; the concept of privatisation process in TBF; the factory’s management and structure; the accounting information system; the budgeting system; the cost and pricing system; the reward, penalty and accountability systems; an assessment of the factory’s effectiveness; and finally a summary of the chapter.

#### **8.1 An overview of the factory’s history**

The factory was established as a company in 1970, with actual work starting in 1971 and on the 1<sup>st</sup> of September 1989 the factory became owned by its employees, under the Libyan privatisation experiment. It is now operated by a People’s Committee, which executes the day-to-day plans and policies, and a Congress Committee, which supervises the main activities of the factory. These produce different types of brick for walls and ceilings using the main raw material (clay), which is locally available in large quantities. The targeted production of the factory is 50,000 tons of standard bricks per year, which are sold directly to the consumer (such as individuals, private building companies etc.), without any middlemen.

#### **8.2 The concept of privatisation in TBF**

Privatisation, from the Libyan people’s point of view, means changing the ownership of the factory from the public sector to the private sector, any previous labourer becoming a shareholder. The Head of the Accounting Department stated that privatisation in the



Libyan experiment meant that “the producer who was a labourer in the past now has a share in the factory instead of a salary and he has the right to participate in the decision-making process of the factory.” This right was envisaged as giving an incentive to all the producers to exert more effort to increase profit. Thus, there is a change in the organisational objectives towards profit-making. The Director of Financial and Administrative Affairs also mentioned that the Libyan privatisation is a kind of ‘gift’ given to the producers to encourage them to increase production and attain self-sufficiency. In addition, the Secretary of the Congress Committee stated that:

“The privatisation process is a kind of guarantee for the producer to have a share of the proceeds of the factory in return for his efforts. Privatisation of this sort truly adheres to the saying from the Green Book that ‘those who do not work are not eligible to eat with the exception of those who are incapacitated’.

### **8.3 The factory’s management and structure**

This section is divided into two parts: the first part deals with the relationships between the factory management and its environment and the second one considers the internal relationships between the management and the other parts of the factory (see Figure 8.1).

#### **8.3.1 The management and its external environment**

The nature of the relationships between the factory and the Tripoli municipality ministries is not clear cut and lacks the understanding that a smooth flow of information would provide. The reason for this could be the absence of any clear official lines of communication that would reveal the nature of the relationship between the factory and other state bodies such as the Ministry of Industry. At the same time a direct relationship exists between the factory and the Ministry of Industry of the Tripoli municipality. This is because after its privatisation the factory fell under the supervision of the ministry whereas previously it used to be a part of it. The Ministry of Industry still plays a significant role in the daily production processes within the factory by involving itself in the administrative affairs and production policies of the factory and



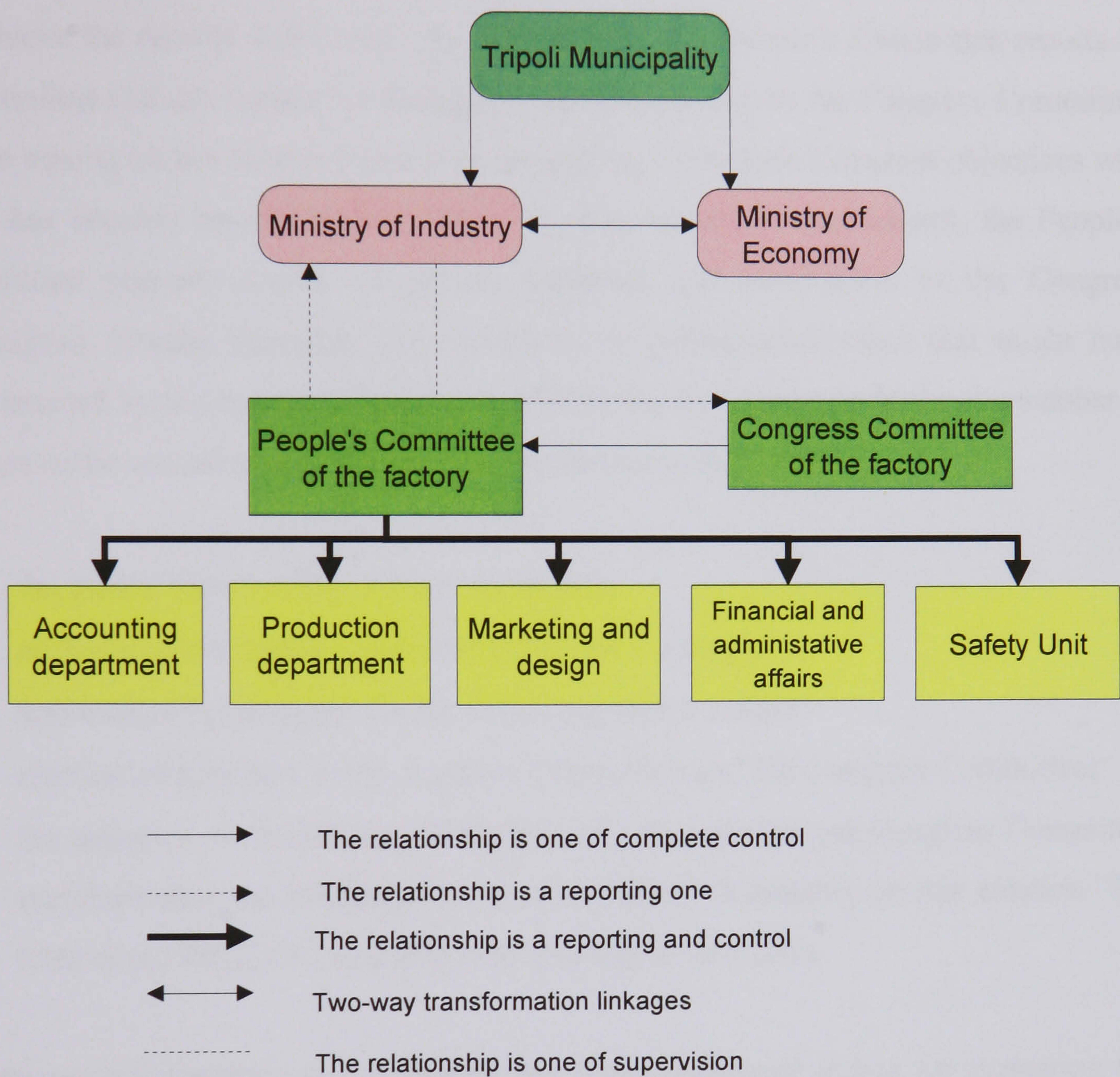
attempting to impose regulations which do not form part of the privatisation contract as these imposed regulations prevent the implementation of the privatisation contract rules. Obvious examples of interference are in the pricing policy and the import budget (see sections 8.5 and 8.6).

The Ministry of Industry interference may be mainly a result of a lack of clear directions, duties and responsibilities of this Ministry. An example of this interference is the influence on the appointment of the chairperson of the People's Committee in the factory from the five members. By doing this, the Ministry exerts a direct influence on the factory's activities and through informal procedures the Ministry has, in effect, appointed the factory's manager. It can be therefore concluded that the Ministry of Industry still maintains a role in controlling the day-to-day processes in the factory, and the role of the factory management seems to be somewhat limited in scope. Consequently, there is a conflict and contradiction between written rules and policies, as the written rules emphasise that the management has the right to manage and control the factory independently, whereas what is in reality taking place is that the Ministry of Industry is managing and controlling the factory. The Ministry of Industry still acts as though the factory is state-owned and this is an important cause of conflict.

### **8.3.1 The management and its internal environment**

The management of this factory consists of a People's Committee with a chairperson and four members. This committee is elected by the employees to manage, control and plan the activities of the factory in order to achieve the factory's objectives. The committee has an administrative staff to achieve and control day-to-day jobs such as financial processing, computing, budgeting, banking, inventory control, product control and pricing. There is a set of written rules, procedures and policies in the privatisation contract that is used to guide People's Committees as they administer their departments (see Figure 8.1 and Appendix A). All employees are members of the Productive Congress, which elects both the Congress Committee and the People's Committee.





**Figure 8.1: The structure and the communication and control linkages in TBF.**



According to the contract of ownership, every employee in the factory holds the same number of shares in the factory as every other employee in the factory. The Congress Committee represents the Productive Congress by way of being a controller to the People's Committee of the factory to ensure that the latter executes the factory's plans to achieve the desired objectives (see Figure 8.1). The People's Committee reports on all activities that are conducted through its administrations to the Congress Committee. It also reports on the control process by comparing Productive Congress objectives with what has actually been achieved. Also, in terms of day-to-day control, the People's Committee presents copies of all its decisions and resolutions to the Congress Committee, thereby exposing any deviations or maladministrations that might have been enacted by the People's Committee. The Productive Congress looks at a number of matters in the annual general conference, which are as follows:

- the annual report of the factory's activities;
- approval of the balance sheet and the income account;
- approval of the proposal for the following year's budget;
- election of members of the People's Committee and the Congress Committee;
- the approval of the election of the People's Committee and Congress Committee members after the confirmation of the Ministry of Industry on this election. The term of the People's Committee membership is five years.

The People's Committee of the factory has many additional duties for managing the factory and these are as follows:

- preparing plans and programmes to achieve the factory's objectives;
- preparing the budget proposal for the coming year and the budget for the current year;
- provision in respect of buying of all production process needs such as raw materials, spare parts and other essential items;
- controlling and improving product marketing;
- preparing training programmes for the workers.



From Figure 8.1 it can be seen that the relationship between the People's Committee and its administrative departments is one that is managing and controlling in nature. The People's Committee of the factory draws up the policies and rules—policies and rules, through the implementation of which it is hoped that the Congress Committee will attain the factory's aims and objectives. All departments are directed by the People's Committee to attain these goals and correspond with the People's Committee regarding any departure or contradictions until the source of these contradictions is identified and remedied, so any mistakes can be avoided and co-ordination kept between the system units. The Productive Congress is invited annually by the Congress Committee to the factory's annual general meeting for the presentation of the annual report of the factory's activities. In this accountability and assessment meeting, the People's Committee presents a detailed report about all activities in the factory and what it has achieved in the previous financial year, and highlights all operations and proposals for the coming year. Also, financial accounts are reviewed and inspected for approval.

The Productive Congress has the power to convene to replace any member of the People's Committee or the Congress Committee and approve any changes in the plans or policies of the factory (see appendix A). From the written rules and policies the Productive Congress has the right to replace and appoint any member of the People's Committee or the Congress Committee at any time. The actual process however, is in practice complicated because this kind of process requires approval from the Ministry of Industry. Furthermore, the Ministry of Industry has on many occasions become involved and has appointed the chairperson of the People's Committee. Consequently, all parts of the factory (system) are likely to have an unclear vision with regard to their rights and duties in respect of the managing and the controlling of their activities.

The People's Committee is duty-bound to prepare a report on the progress of work to be presented at the general meeting of the Productive Congress held every year. The role of the factory management is not successfully carried out with ease because it is in fact very difficult to persuade producers to comply with the rules and procedures. The producers hold the opinion that nobody has the right to impose such rules and



procedures on them since all producers should enjoy the same rights and duties. This inertia among the producers regarding the objectives of privatisation hinders and weakens the management role. Consequently, the management is actually trying to adhere to the concept of the producers as the producers elect the management members, yet this concept often prevents them from practising their jobs after they have been elected. Also, with regard to penalties and rewards, it can be concluded from an inspection of the records and the management reports that no penalties or rewards were given to any producer, and there was consequently no competition among the producers in the factory. An expert in the privatisation process in the Ministry of Industry described the feelings of the producers in the factories as being that “every producer has the feeling that he is not supposed to be liable to give any explanation to other producers or the management.” This kind of idea provoked and raised the tension between the management and the producers, owing to the misunderstanding of the rights and obligations of each producer. Each producer tries to get office work, and posts requiring physical exertion are no longer attractive. This is why the door was opened to employ foreign labour (the Secretary of the People’s Committee).

This contradiction between supposed responsibilities and actual duties is one of the largest problems that privatised factories face. Through an observation of the research site the researcher realised that the Secretary of the Treasury of the factory also held the post of the Secretary of the Congress Committee. According to official documents such as the ownership contract, that post should have been a separate post as it is a controlling and supervisory post. The Secretary of the Congress Committee is supposed to supervise the People’s Committee, whereas the post of Secretary of the Treasury is an integral part of the People’s Committee. Therefore, there is a contradiction between the functions of the two posts. The Secretary was asked about his role in the monthly and annual meetings of the factory. He replied by saying that:

“[W]hen the subject deals with the administration only, I take the platform as the Secretary of Treasury, and when the issue deals with the factory as a whole I take the platform as the Secretary of Congress Committee. Moreover, the post of Secretary of the Treasury gave me the chance to see the returns of the factory and its expenditure before anyone else”.



During the researcher's stay in the Treasury section, it was observed that the post of Secretary of Treasury took all this person's time and he spent most of his time in this section, to the exclusion of the duties of his other post. Most producers and customers knew him as the Secretary of the Treasury and not as the Secretary of the Congress Committee.

#### **8.3.1.1 The factory's workforce**

The labour force in the factory is not large enough actually to run the factory, and according to the law, this shortfall in skilled personnel is covered by resorting to experts from outside the factory. These experts are employed on a local contract basis and for a fixed term before being released. The problem of contracts is that these labourers are paid salary, without any shares, a practice contrary to the principle of the privatisation process, which aims at treating all Libyans equally as shareholders. The Production Manager described the factory's workforce by saying that:

“The number of untrained and unskilled labourers is far higher than the requirements of the factory. These surplus unskilled labourers are a burden on the factory from both a financial and administrative point of view”.

For instance, the Ministry of Industry refers some labourers to the factory for employment without any prior investigation to ascertain the actual needs of the factory for such labourers. In most cases these labourers are inexperienced and unskilled and add to the financial and administrative burden of the factory. This action causes damage to the productive system (see Table 8.1). The Production Manager referred to the fact that there were more than 10 labourers in the production department who have no posts and they had been appointed through personal relations. He continued that “the situation in the production department is critically bad, there are surplus labourers, but so long as the financial situation in the factory is good we also do not want to fire anybody.”



Table 8.1: The workforce in The Bricks factory in 2003.

The workforce number					Added Employees		Expelled Employees	
Libyan		Personal contracts	Technical contracts	Total	Male	Female	Male	Female
Male	Female							
85	2	22	5	114	-----	-----	-----	-----

Source: The workforce report, 2003.

The Secretary of the Productive Congress mentioned that one of the advantages of the privatisation process was that the shareholder was considered as a self-controller for the labourers appointed by contracts. He said that:

“I paid a surprise visit by night to the factory and I found work progressing perfectly and without any supervision. This is an indication that the shareholder feels that he is working for himself and therefore, he works harder and urges other to do the same”.

8.4 The role of the accounting system

The role of the accounting system is to provide information and data for the management to enable it to take decisions at the proper time (The Secretary of the People’s Committee), a role that has continued throughout the privatisation period. The only difference to appear in the accounting system after the privatisation process was that the producers started to pay more attention to the financial situation of the factory. They tried to understand all the administrative and financial issues, knowing that they were shareholders and thus the owners of the factory. The head of the accounting department, who spent 15 years in the factory, commented on this by saying:

“Previously (before privatisation) the workers paid little attention to the financial information or whether the factory was making profits or losses. Yet now (after privatisation) the producers request an explanation for all figures in the budget or in the income statement and also the items of expenditure and how the net income is calculated.”



All items of the budget are now discussed in the Productive Congress in its annual meetings; producers decide on the budget for the current year and propose the budget for the coming year and all financial information plays a dominant role in decision-making. The management frequently asks for information relevant to bank settlements, available cash and sale of assets, so as to evaluate the financial situation of the factory before taking any decisions with regard to purchases or sales (the Head of Accounting Department).

As far as the applications of accounting are concerned, very few changes have taken place in the accounting system in the factory, with the exception of the establishment of a special account for the distribution of profits among the producers. Each producer has a separate page showing the annual value of his shares, the number of shares from the capital, and the dates of the securing of these shares. The Director of Financial and Administrative Affairs argued that “after the privatisation process a new relationship between the shareholder and the factory appeared, because every producer now felt that he was a part of the factory.” It is possible that the factory may face some problems in the future; problems that were not very accurately anticipated by the regulations and bylaws. These are, for example, the problem of joining or withdrawing from a shareholding and what the exact size of the value to be paid to the withdrawing producer or to be paid by the joining producer is. This is necessary as the withdrawing shareholder may ask for an evaluation of the entire factory. One of the accountants argued that “if a shareholder who is withdrawing asked for an overall evaluation of the factory, this would mean liquidation of the factory” (as the factory would have to be closed for evaluation in order to determine the value of his shares). Other producers may also withdraw and the factory would be faced with a series of stoppages for such withdrawal applications. The same problem also arises when shareholders would like to join the factory, yet none of these issues were specifically addressed in the regulations governing privatisation. Consequently, there is no formal or efficient handling of these issues when they are faced. One of the producers in the production department expressed his views on the withdrawal of producers from the factory by saying: “A bird in the hand is better than ten on the tree.” Among the producers there is no trust in the resolutions and regulations issued by the state. The factories may be returned back to



the state in terms of re-nationalisation and hence the producer would lose his shares in the factory.

In order to improve and develop the present accounting system in the factory, the Head of the Accounting Department suggested using a special reserve fund, allocated from the profits every year. This should provide for the development and replacement of equipment and the purchase of new machines to improve production capacity. This proposal was rejected to by the producers because they insisted on distributing the profits every year and refused any capitalisation of the profits. This objection is arguably owing to a lack of understanding among the producers of the importance of maintenance and replacement and its role in increasing productivity and profits. Since the producers have elected the members of the People's Committee and the Congress Committee, they believe these members should respect the will of the producers and consequently, the idea of profit capitalisation is rejected. The Secretary of the Congress Committee referred to the ignorance of the producers with regard to the importance of the capitalisation of profits as being the cause of the producers not understanding the long-term targets of this idea. Also, the producers did not trust management procedures and thought that every action to maintain profit was merely manipulation. The Secretary of the Productive Congress described the lack of understanding and the educational level of the producers thus:

“The discussion of the budget takes several weeks or even months in the Productive Congress meeting. Nevertheless, many producers claim that they do not know anything about these items. If there was any awareness among the producers, the condition of our factory, our machines and equipment would not be getting out of date and old”.

It can be concluded that with the absence of a Libyan stock market, the only channel for the producers to find out about value and profit of their shares is the accounting system. Accounting is becoming, for instance, the single information source and more of a distributive mechanism. This change in the significance of accounting for the producers raises a need for improvement in the role of accounting system in privatised factories in order to satisfy the producers' needs.



### **8.4.1 Accounting records**

In Libya, there are legal requirements for enterprises to keep records of their activities. According to the Libyan Commercial Code (LCC), each company or enterprise must have at least the journal, inventory and balance sheet to record and illustrate its activities (see Chapter 4). These records are very important to both the enterprise and the state in order for example to identify and calculate national insurance and pay taxes. Furthermore, these books and records can provide information about the current situation of the accounting practices in the enterprise and this information can be used for planning and controlling activities. Unfortunately, the accounting department prepares the financial statements for state requirements and most of the accounting to record the transactions is still done manually. The accountants use the same financial statements for both the needs of management and external parties. These procedures and stages of the accountants' job have not been changed since the time of Bait El-Mal *et al.*'s study in 1988, when they concluded that most of the required financial statements of the Libyan companies were prepared for the purpose of Tax Law. Also, the low demand for financial statements prepared using different bases has led Libyan companies to prepare the same set of financial statements for both internal and external purposes. This situation does not provide the varying types of accounting information needed for both internal and external needs.

## **8.5 The budgeting system**

The Head of the Accounting Department argued that there was no system for applying the estimated budgets in the factory. Indeed, only the operational budget, which contains the requirements of the factory for things such as spare parts equipment and machinery for the coming year, was drawn up. This was done to satisfy legal requirements and certain parties such as the Ministry of Industry. One of the accountants mentioned that "budgets are done only on paper and not practically applied. We usually copy the same figures from the previous budget with some minor changes to the figures but not in the items." These budgets are not used in daily work, and no comparisons are made between the actual work and the budgeted work (which is set as the expected work) because the estimates were baseless (according to the Head of the



Accounting Department). Indeed, the only budget that was prepared and approved was the operational budget; it was approved by the management of the factory and sent to the Ministry of Industry in Tripoli Municipality. This was because it contains the imported items, and it is used to determine the share of foreign currency allocated to the factory from the state import budget. Unfortunately, only very small quantities are allocated; much less than the actual needs of the factory. This is because the people in the Ministry of Industry apparently do not actually study the real requirements of the factories.

In fact, the actual distribution (allocation) of funds between the Ministries in the municipality takes place in secrecy (the municipality allocation from the state budget is received by identified people in the municipality) between certain individuals. Once the Ministry of Industry receives its allocation from the municipality import budget, formal and informal connections and relationships between the management of the factories and the Ministry of Industry play a significant role in the allocations of the foreign budget (hard currency). As a result of this, and the absence of any clarity in the administrative chain of responsibility between the Ministry of Industry and privatised factories, the Director of Financial and Administrative Affairs argued that:

“[U]nofficial relationships play an important role in setting the share of each factory. Consequently, some factories exaggerate their requirements of imported materials by listing and recording astronomical figures in the budget in order to be allocated sufficient funds of foreign currency”.

Hoque *et al.* (1994, p.429) in their study stated that “managers often overstated their estimates to compensate for anticipated cuts to protect their (factory) in the struggle for resources.” The Production Manager expressed his dissatisfaction by saying that the distribution of foreign funds was unfair. He mentioned that:

“A bakery which employs one person may get more foreign currency per year than our factory gets, because the bakery uses its personal contacts in the Ministry of Industry in the Municipality to influence decisions about the allocation of foreign currency”.



These actions have direct implications for the production process, since the factory was unable to buy its spare parts and equipment, and this was reflected in the low productive capacity and the maintenance of its machinery. The factory becomes subject to stoppages whereby it experiences big losses in production (according to the Production Manager). Tables 8.2 and 8.3 show the production capacity and the foreign currency allocation of the factory for the year 2000.

Table 8.2: The production capacity of The Bricks factory in Libyan currency in 2000.

Particulars	Unit	Designed capacity		Targeted production		%
		Quantity	Value (LD)	Quantity	Value (LD)	
Bricks	Ton	55,000	2,946,000	50,000	2,675,000	90%

Source: Accounting statements, Accounting Department, Tripoli, 2000.

Table 8.3: The factory’s foreign currency allocation in 2000.

Particulars	(LD)	(LD)	Total (LD)	%
Operational budget (targeted production)	Spare parts	Machines		
	150,000	500,000	650,000	
Foreign currency allocation 2000			273,000	42%

Source: Accounting statements, Accounting Department, Tripoli, 2000.

Once all the above procedures are completed, the factory administration enters into another administrative cycle, which involves the Ministry of Finance and the Central Bank of Libya. This is where the Ministry of Finance through the Ministry of Industry imposes a string of administrative regulations until the matter is referred to the Central Bank. The Central Bank determines the exchange rate between the LD and the US dollar (LD0.45 = \$1.0) and this official exchange rate is different from all other banks and the black market<sup>29</sup>. These differences in the exchange rate led to a shortage in the foreign currency available to the factory management. The next step is for the authorisation to be sent to the External Bank, and this procedure is somewhat lengthy (it takes a long time because the Central Bank is the only channel for approving the import



process). The complexity of this process and its time-consuming nature leads to the factory management forging unofficial contacts and relationships in order to catalyze this process, as any delay in the importing process directly affects the factory's day-to-day operations. Hence, according to the Secretary of the People's Committee, dependency on these unclear relationships probably means the management of the factory is unable to plan and control its activities.

## 8.6 Cost and pricing system

The sales process is only for the finished product, i.e. the bricks, and the final selling price is determined by the Ministry of Economy in the Municipality. The internal accountant is responsible for calculating the cost of the production components; this calculation of the product cost is reviewed in the accounting department and the final cost statement is sent to the pricing department in the Ministry of Economy for approval and for a determination of the profit margin in order to decide upon the final selling price. The profit margin needs to be re-evaluated however, especially in the present circumstances when the sources of raw materials have come under the scope of other municipalities. A detailed report about the reasons to change the profit margin was prepared by the factory to support the claim for change. This report might take a long time to be addressed and again it is often the case that informal (unofficial) relationships could affect any speeding up or delaying of this process. The Head of the Accounting Department argued that the determination of the profit margin by the Ministry of Economy of Tripoli Municipality was not the outcome of either any study or investigation of the factory's needs (which affect the production processes), or of the factory's obligations, liabilities and market. In the absence of such studies and consideration, the profit margin is not always sufficient to enable the development and improvement of various activities in the factory. These procedures (regarding profit margin), which were not part of the official procedures stated in the privatisation contract of the factory, probably led the factory administration to consider distorting the calculations of the production cost so as to depict a realistic profit margin. The procedures of adjusting the profit margin thus take a long time, and this has a negative

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<sup>29</sup> A black market exists because of the limited channels for foreign currencies in the country.



impact on the production process. Table 8.4 shows the calculation of the cost of the bricks:

Table 8.4: The calculation of the cost and the price of the product in LD in 2002.

Subject	Partial	Total
Spare parts	270,000	
Petrol	70,000	
Maintenance	30,000	
Travel expenses	10,000	
Electricity	40,000	
Rent	12,000	
Wages	345,000	777,000
Fixed assets depreciation		169,000
Administrative expenses		386,980
The cost of clay		100,000
Total of the expenses		1,432,980
Actual production of 2002	Ton	32,000
Cost of one Ton		44,781 LD
Cost of one metre		3,135 LD
The sale price of one metre	$3,135 + (3,135 \times 15\%)^{30}$	3,610 LD

Source: The accounting statements, Accounting Department, Tripoli, 2002.

The actual production figures are used as a base to calculate the cost and the sales price of the product because the targeted production is not always achieved. According to the research evidence, the factory is 100% dependent on local raw materials. It can therefore be concluded that the shortage of imported raw materials and exchange rate of the LD against the foreign currencies has little effect on its production.

<sup>30</sup> 15% is the government profit margin.



## 8.7 The reward, penalty and accountability systems

Because of the lack of authority of the management of the privatised factories and their inability to apply the bylaws of such a system, the management was not able to apply the system of rewards and penalties in the factory. The producer is convinced that he is equal to others and nobody has the right to impose any sanction on him (the Director of Financial and Administrative Affairs). One of the accountants stated that:

“[W]hen deducting one or two days from the producer’s salary, it may take a very long time to convince him, and he asked the management to guarantee that no such deductions will be made without good reason”.

There are no systems in place for rewards either and this is why they are never paid. Unfortunately, even overtime payment systems were not practised. Hence, all kinds of incentives for developing and increasing production were abandoned. There were no meetings for impeachment or accountability between the factory or any other external authorities such as the Ministry of Industry, though monthly reports were sent by the factory to the Ministry of Industry in the municipality. These were intended to supply the ministry with information about the actual production and the labour situation and whether there was any diversion from the targeted production. The Production Manager stated that the Ministry of Industry was informed about the reasons for not achieving targeted production, the most important of which was the shortage in foreign currency for the import of spare parts and machinery for which the Ministry of Industry itself was responsible.

At the factory level, plans are distributed to all departments, detailing the targets and objectives to be achieved by each department. Every department should prepare a monthly or quarterly report showing its ability to achieve the targets, and from these reports the departmental representative can be questioned in the People’s Committee meetings. Since all heads of departments are members of the People’s Committee this is meant to help in the realisation of the targets (the Director of Financial and Administrative Affairs). The Secretary of the Congress Committee stated that joint



meetings were held between the Congress Committee and the People's Committee at least once a year to question the People's Committee and hold it accountable for some issues in the factory and also to address any difficulties the factory was facing. For example, in the year previous to the year in which the research was conducted the production was stocked up while demand was very low. A meeting of the People's Committee was called to discuss the problem and explain the reasons that had led to this situation and solutions were suggested to avoid such situations in future. These solutions were placed before the meeting of the Productive Congress in its annual meeting.

## **8.8 Assessment of the factory's effectiveness**

It can generally be said that the factory succeeded in achieving most of its objectives and targeted plans. This success is evident in the achievement of the targeted production objectives on many occasions since the establishment of the factory. The Secretary of the People's Committee and the Production Manager stated that the factory had often achieved its targeted production during its life because of the availability of the raw materials in the country (see section 8.4). Consequently, the factory had successfully met the local demand for bricks. As a result of its dependency on local raw materials, the factory was little affected by state procedures regarding the import budget; indeed, spare parts and new technology were the only parts that the state still controlled. Nevertheless, shortages of spare parts and machinery on occasion led to the factory failing to meet the local demand in terms of product quality in order to compete with imported products. There were many internal and external factors that affected the autonomy of the factory's management. The shortage of spare parts and state intervention in many of the factory's activities (such as pricing, budgeting and imposing high taxes) contributed to this partial failure.

The factory's failure to achieve some of its objectives is the result of a lack of experience and education among people in the factory, preventing understanding and awareness of the factory's objectives as a means of achieving the future plans (see Chapter 9). The central figures in the study were the Secretary of the People's



Committee and the Director of Financial and Administrative Affairs who had been working in their posts for around 10 years and were managing and controlling everything in the factory. All people on different levels in the factory sought their approval, even for routine processes, before doing anything. Hence, a maximum amount of personal control over the factory was maintained by the Secretary and the Director.

To summarise, the factory could be described as satisfying its employees, management and (assumed) environmental needs of its products even though the factory still failed in achieving certain objectives such as consistent product quality, employee training and capital investment. The working conditions were very poor and the safety procedures were very limited. Also, old technology was still used in the factory and there was a shortage of foreign currency for spare parts. All these factors led to the factory's partial failure, and there were no plans for future investment to improve the efficiency of the factory, yet the factory has a good reputation for producing bricks and providing them for half of the country.

## **8.9 Summary**

This chapter provided a discussion of the existent MCSs in TBF. The answer to the question of how people in the case study perceived and used accounting information was elaborated. A discussion of the MCSs in TBF was presented to highlight the important issues regarding managing and controlling the day-to-day activities and to provide a chance for a holistic understanding of the MCSs in the factory. Moreover, the kind of information available for managers (the People's Committee) in order to achieve the factory's objectives was considered and elaborated. This chapter highlighted the influence of the state in day-to-day affairs and the implication of this intervention on the nature of the MCSs in the factory. It was apparent that the factory avoided the problem of imported raw materials as it depended 100% on local raw materials. However, the Ministry of Industry and the Ministry of Economy, for instance, play a vital role in many functions such as budgeting and pricing.



## **Chapter 9: Discussion and Analysis**

### **9.0 Introduction**

The three case studies were analysed drawing on systems ideas and following an interpretive perspective emphasising qualitative methods. Here, the concern is to analyse and discuss the cases with an emphasis upon the significance of the contextual change. Comparisons are also made between the findings across the three cases, with an elaboration of similarities and differences. For Yin (1994, p.34), the development of consistent findings over multiple cases contributes to more robust findings. Here, the differences between the detailed case studies is also of interest.

### **9.1 Organisational objectives**

In all the factories studied, there was no clear appreciation on the part of the personnel that the introduction of the profit motive by the state was an attempt to achieve wider objectives of for instance, greater self-sufficiency of essential products. Moreover, the management did not have any substantive plans to achieve, or procedures to guide them towards achieving, such objectives as understood in terms of state policy in the new era of privatisation. For instance, the Director of Financial and Administrative Affairs of the LFF argued that production had increased almost three times in the last decade, but seemed unaware that the issue was not only a matter of production quantity but also a matter of considering how this level of production affected and is affected by demand, price and other market forces. His understanding was more production orientated than profit orientated. It was found, in general, that the state objectives regarding the privatisation process were apparently designed to encourage profit orientation so as to enhance Libyan self-sufficiency in essential products, but an understanding of these objectives at the factory level, according to the data this researcher collected, was very limited. The Secretary of the People's Committee at ANF reported low internal awareness regarding the objectives of the factory. It can be suggested that the failure of



these factories to achieve their targeted production over the period covered by this study (see Tables 9.1 and 9.2) was at least in part a result of the producers' lack of focus upon and misunderstanding of the organisational development objectives. Table 9.1 suggests that there was an ambitious aim to grow and expand in the exportable industries by setting high targets for production. However, these objectives were restricted in practice by the state centralisation of vital organisational functions such as pricing and budgeting (see sections 9.5 and 9.6).

Table 9.1: Production report in respect of the privatised factories, 2001.

The factory	Unit	Targeted production	Actual production	% Achieved
LFF	Ton	13,693	1,566	11 %
ANF	Pad	84,538,000	9,607,600	11 %
TBF	M <sup>2</sup>	50,000	30,000	60 %

Source: Production Report, Industrial Sector, Tripoli Municipality, 2002.

Table 9.2 shows the stoppage of the production process as a result of the implementation of the state policy. All the factories under study had to stop their production process as a result of shortage of raw materials, spare parts or supply of utilities. This stoppage time can be linked to external circumstances such as the state-centralised administration of imports (see sections 6.4, 6.5, 7.5 and 8.5). Consequently, it had a negative impact on the management and control functions in these factories.

Table 9.2: Stoppage hours in the privatised factories, 2001.

The factory	Stoppage hours (per year) by reasons for stoppage				Total stoppage (hrs)	% Downtime <sup>31</sup>
	Raw materials shortage	Spare parts shortage	Technical Issues	Electricity shortage		
LFF	1,480	0	0	0	1480	52 %
ANF	174	0	58	0	232	8 %
TBF	0	80	130	240	450	16 %

Source: Industrial Sector Report, Tripoli Municipality, 2002.



To recapitulate, a lack of clear written objectives for the privatised factories and a lack of understanding and awareness on the part of the producers of the state's objectives with respect to these factories is threatening in that the factory management lose one of the most important means of motivation—objectives. This lack of understanding and awareness was arguably a result of the misunderstanding among the producers regarding the objectives of the state privatisation experiment (see Chapter 5). The producers, partly because of a lack of awareness, partly because of uncertainty about the future and partly because of a lack of trust, which engendered a lack of identification with the state policies and procedures, sought short-term benefit from the privatised factories (profit distribution instead of capitalisation). This finding agrees with that of Smallbone and Welter (2001, pp.64-65) where they stated that “a number of transition economies suggest that factors such as interest rates, as well as a lack of trust regarding private property rights, can discourage entrepreneurs from making long-term investments, encouraging them instead to engage in activities with high turnover and relatively high profit margins but low thresholds.” In this context, perhaps it is not surprising that the achievement of the state's privatisation objectives was very limited (see Chapters 6, 7 and 8). Furthermore, this kind of contradiction between the state at the top and producers at the bottom hinders the development process in these factories and prevents the achievement of what the state ostensibly desires.

## 9.2 Ownership

The change in the nature of the ownership of these factories took place according to state decisions regarding transferral of the ownership of a group of public organisations to their employees with the aim of expanding and improving the role of the private sector and reducing the dominance of the public sector. The main aim of this process was ostensibly to develop the industrial sector in terms of efficiency and effectiveness and achieve greater self-sufficiency in essential products such as food, building materials and paper products (see Chapter 5). The process of change created serious

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<sup>31</sup> The working hours are 10 hours x 280 working days in the year = 2800 hours.



problems at both the factory and the wider economic level. It would appear that the state did not adequately consider the actual situation of these factories and the consequences of these changes, nor did it provide appropriate solutions to problems such as a surplus workforce or inadequately skilled management of the factories. Furthermore, as a result of informal relationships between individuals in the companies and state ministries, it is suggested that unskilled people became managers and controllers of relatively large amounts of capital. Additionally, there was a lack of education and experience amongst the employees (the owners). From the perspective of this author, and based on the analysis, it may be seen that employees who had a close personal relationship with the Ministry of Industry were substantively controlling and managing the activities of these factories. Moreover, these employees were expected to comply with the state policies reflected at the level of the People's Committee and Congress Committee established in these factories to manage and control the day-to-day processes (see Chapter 4). To recapitulate, there is a lack of understanding of the state policies by the people at the factory level as a result of a lack of experience or awareness of the ownership policies and procedures. Related to this lack of awareness of the privatisation objectives on the part of producers (see sections 6.3, 7.3 and 8.3), is the fact that all producers want to be members of the factories' management, perceiving themselves to have an equal number of shares and thus having equal rights. This desire for ownership has led to difficulties in managing, controlling and implementing regulations.

### **9.3 The structure and management**

All the factories in the case studies have similar formal structures and management. The management of all the factories consists of five members forming the People's Committee who are selected as a result of an annual election in the factory by the Productive Congress, which represents all the producers in the factory. One of these members is the chairperson (manager) of the People's Committee (see Figures 6.1, 7.1 and 8.1). The People's Committee is elected to manage, control and execute the factory's plans and policies in order to achieve the factory's objectives. The Productive Congress also elects another committee called the Congress Committee, which functions as a representative of the Productive Congress to supervise and control the



People's Committee to ensure that the latter is executing the factory's policies and plans effectively. The People's Committee has both an administrative staff and departments to undertake and control the day-to-day activities of the factory.

According to written documentation such as the ownership contract (contract of sale between the government and the employees), the People's Committee has a number of specific duties to fulfil (see Chapters 6, 7 and 8). It reports to the Congress Committee on all the factory's activities and the factory's progress in achieving its objectives. It also presents at its annual meeting the factory's achievements of the recent year and its projects for the following year to the Productive Congress. The formal relationship between the People's Committee and its departments is one of management, control and accountability (the People's Committee could call to account all its departments at any time) and the departments must report to the Committee with regard to any problems or in respect of achievement of objectives. From written documents, such as the ownership contract and the development plans (see Appendix A), it appears that the Productive Congress has the right to change, replace, stop, abolish, develop and also bring to account any plans, rules, positions and activities in the factory as a private organisation. Accordingly, the Congress Committee as a representative of the Productive Congress has delegated rights such as being able to bring the People's Committee to account and convene the Productive Congress to meet if it finds any serious problems in the factory (see Appendix A). From this researcher's investigations, the actual situation in the case studies differed significantly from the written documentation regarding the formal structure (the ownership contract between the government and the employees being the important document in privatised factories), as elaborated in what follows.

In case one, it was apparent from the observations that the Secretary of the People's Committee and the Director of Financial and Administrative Affairs were the key managers in the factory and that the Congress Committee had only a limited role in terms of control. The final decisions regarding any subject in the factory were made by these two key people. The participation of the other People's Committee members in any decision-making was very limited, because most of the factory's affairs were discussed in the office of the Director of Financial and Administrative Affairs, with



discussion taking place between the Director and the Secretary of the People's Committee. These two key people had been working in their posts for at least 8 years, yet during this time no reports had been prepared for the Congress Committee and from the investigations it emerged that no accountability meetings had been held involving the People's Committee and the Congress Committee. On many occasions, the Director of Financial and Administrative Affairs had acted as the manager of the factory yet he has, according to the written documentation from the government, no right to do so, as the state rules show that in the case of the manager's absence one of the remaining members of the People's Committee becomes manager. This situation could be interpreted in a number of ways. Is it a lack of understanding of the rights and duties among the Congress Committee's members and/or the whole Productive Congress? Is it because of the impact of strong social and personal ties on the election of the People's Committee members? Is it because of a lack of appreciation of the rules and regulations explaining the relationships between different parties inside and outside the factory, thereby affecting the function of control in the factory? Based on the analysis of this research, the lack of understanding of the rights and duties among the People's and Congress Committees' members, the impact of informal relationships and the lack of appreciation of the rules and regulations between internal and external parties all have contributed in shaping the current MC functions in the factory.

In case two, the Secretary of the People's Committee had been working in this post for 13 years and was the key person in the factory who made the final decision in respect of most of the factory's affairs. The Congress Committee had again a limited control role as they considered themselves weaker than the members of the People's Committee. This perception of weakness was a result of the fact that all their financial and administrative problems tended to be solved in practice by the People's Committee. They themselves (the Congress Committee) had little influence with regard to the solving of these problems. Most of the Congress Committee members have actually received personal facilities such as loans from the People's Committee, tying them to the influence of the People's Committee. The Secretary of the People's Committee described the role of the Secretary of the Congress Committee as follows: "the Secretary of the Congress Committee has no practical role except on paper. The



Secretary of the Congress Committee receives many personal facilities (e.g. loans, cars). These facilities hinder his ability to criticise the People's Committee. By doing this, we avoid the problems of changing the members of the People's Committee." From this research, this can be explained and interpreted as follows. Personal relationships played quite a significant role in the election and continuance of the Committee members. Certain people who were not experienced and were relatively unskilled came to hold influential posts and became members of the factory's management. As a result the planning and control functions were largely under the jurisdiction of such individuals and were hardly likely to be conducted effectively. Further, this inertia stems from the absence of any substantive internal bylaws regulating the work and determining the rights and liabilities of the personnel and management of the factory. Thus, the formal management structure in the factory was quite unable to implement any policies or regulation in order to achieve their targets.

In case three, once more the Congress Committee had a limited role in controlling functions in the factory. In the studies, it was found that the Secretary of the Congress Committee was working as a treasurer under the control of the People's Committee. Consequently, any controlling role of this person (as a Secretary) was restricted. The Secretary of the People's Committee was the key person in the factory and he had been in this post for 10 years. Yet again, as in case two, no accountability meetings were held involving the People's Committee and the Congress Committee and no reports were prepared by the People's Committee for the Congress Committee during this time. This could be interpreted in a number of ways: it might be a result of the state party's intervention in the factory's day-to-day activities (for instance, the Secretary of the People's Committee was recommended and appointed by some officials in the Ministry of Industry). Alternatively, it could be a lack of awareness and understanding of the rights and duties amongst the people in charge and the ordinary producers, or a result of the ambiguity of the relationships between the factory's systems and the external environment. Finally, it might be a lack of internal rules and regulations, leading to a misunderstanding in respect of managing and controlling functions amongst the personnel of the factory. From the research, it was concluded that the state party's intervention in the factory's activities, the lack of understanding of the rights and duties



among the People's/Congress Committees' members, the impact of the informal relationships have all influenced the function of control in the factory as has been elaborated in different sections in the thesis (see sections 6.2, 7.3, 8.3 and 10.4).

The formal structure and management of the privatised factories were imposed by the state as an element of policy. This finding creates problems with views such as that of Flamholtz (1983, p.158) that "the choice of an organisational structure represents a managerial strategy on how to adapt the organisational entity to the requirements of its environment". As a result of the state influence, the management in the privatised factories has had very limited autonomy to choose the structure of the management, which directly affected its decision-making function. Thus, managers were unable to manage and control their activities. What is more, the management (the People's Committee) was elected by the producers through the meeting of the Productive Congress, so its ability to confront the producers and implement rules and regulations were very limited.

## **9.4 The accounting system**

All the Secretaries of the People's Committees argued that their accounting systems provided the necessary information for the decision-making function. The Head of the Accounting Department in the LFF insisted that information about production costs, bank accounts, expenses, sales and final accounts was provided to the factory's management to help in managing and controlling the factory. The function of the accounting system in the factories had been expanded to include other functions such as the operation of the marketing department. This additional function (marketing) required more information about prices, customers, debts, supply and demand of products to interact with the market circumstances. The Director of Financial and Administrative Affairs in the ANF noted that most of the accounting information and statements needed for decision-making were available on time. Yet, from the finding of this study, because of failures in the planning and controlling process, it is hard to see exactly what kind of accounting information was requested by the management in the absence of any planning process or clear objectives. Furthermore, accountants collect



market information in an unsystematic way not clearly related to the business but apparently more in the way of proving personal interests. One accountant pointed out that he collected market information not for business decisions but because he just wanted to look at the information. Thus the role of the accounting information in the decision-making function appears limited (see sections below).

In case one, most of the people in charge in the factory insisted that accounting information regarding the factory's activities was available and provided to the management and external parties such as the Ministry of Industry and the Ministry of Economy. The Head of the Accounting Department argued that information about the cost of raw materials and other production elements was gathered in order to prepare the final accounts and statements. The Director of Financial and Administrative Affairs claimed that the accounting system in the factory was good because the final accounts and budgets were prepared on time and without any delay. Further, in response to the question of how satisfied they were with the present accounting system, the Director replied that it was a good system, except that computing facilities had not yet been introduced. However, in fact, the lack of understanding of the role of the accounting system as a source of information for planning and control led to a limitation of the accounting function to just preparation of final accounts. Therefore, the role of accounting information was minimised or seriously restricted (see section 6.3).

The Head of the Accounting Department stated that the general idea of the Libyan privatisation process was to distribute the returns equally between the employees. However, the accounting process and calculations of the profit distribution inside the privatised factories were done differently. There were factories, which were applying the policy of equal return distribution between the employees, while others apply the salary system of law No. 15 of 1981 (see section 6.3).

The accounting cycle in the factory consists of two stages: the documentary phase and the book phase. Although the factory kept some books and records, it seems to keep them only in order to comply with state requests according to the Libyan Commercial Code (LCC). Use of these books as a means of managing and controlling the factory's



activities was very limited. Therefore, there was only limited accurate recording of transactions and only irregular updating of books that could be used as a means of control. The accounting system prepared only one kind of accounting statements, the final accounts. These statements were used for both internal purposes (decision-making) and external ones (reporting to state agencies). There was no cost accounting section in the factory to prepare the cost data as a means of control. This could be interpreted as follows: a lack of understanding of the role of accounting information as a means of control; a lack of skilled personnel (most of the accountants have only a very basic accounting education and experience); these factors compounded by the character of the state intervention in the factory's affairs. As the final decisions regarding most of the factory's affairs were made in the state ministries (budgeting and pricing), all the factory's documents were orientated to comply with and satisfy formal and informal state rules. Hence, the role of accounting information in the decision-making function was limited.

In case two, the Secretary of the People's Committee argued that their accounting system provided useful information for planning and control and that most of the final accounts and statements were prepared without any delay. He added that ANF had an effective accounting system and document cycle as most of the accounting information was available on time. The Head of the Accounting Department mentioned that the accounting system was very simple before the privatisation and that many improvements had to be made to the system in order to meet the demands of the new environment in terms of required accounting information and to help management and control in the factory. These improvements related to stock control and were operated for a limited time before lapsing into disuse as a result of lack of skilled personnel (see Chapter 7). According to the study evidence, therefore, the accounting system still suffered from a lack of skilled people and technology, which was hindering its role as an information provider. Thus, the role of the accounting system in managing and controlling the factory's activities was again limited (see section 7.4).

The Head of the Accounting Department stated that some proposals for improvements in the accounting system and quality of accounting information had been presented in



order to meet the needs of management (see section 7.4). However, most of these changes had failed when put into practice. Therefore, the accounting system still has a limited role in planning and controlling functions. This could be explained and interpreted in a number of ways: a lack of skilled personnel (accountants); inadequate management by unskilled people who had attained management posts by personal relations, not by merit, and consequently had very limited ability to plan and control the factory's activities (as a result, the planning and control function had never substantially emerged in the factory); a lack of understanding of the factory's objectives among the producers, hence the refusal of any proposal for developing the factory's activities (resistance to change) (see Chapter 7); owing to state intervention and the centralisation of the decisions regarding, for instance, product pricing and budget allocation, the accounting statements and figures did not reflect the actual situation of the factory's activities, but were distorted in order to achieve maximum allocation from the ministries.

In case three, the Secretary of the People's Committee insisted that the accounting system provided the necessary information to improve the decision-making function. This function continued after the privatisation process but in the new environment there was a call for more detailed and comprehensive accounting information, and employees in the factory (after becoming owners) asked for more detailed information. At present, there is no cost accounting section in the factory and most cost calculations are prepared by the general accountant who prepares the final accounts by the end of the financial year, the product cost being prepared monthly or quarterly. There were no differences between the accounting statements for internal purposes and the statements for external bodies. This lack of a distinction between the needs of management and those of external bodies led to inadequate accounting information being available for managers to manage and control the activities of the factories. This situation could be interpreted as follows: a reflection of the management's lack of awareness of the accounting role as a means of control, this in turn affecting the quality of the required accounting information; a lack of skilled accountants able to prepare a variety of accounting information according to different circumstances; the fact that most of the accounting statements were prepared to satisfy the state agencies. The external and internal



accounting statements were prepared in the same way and contained similar information, as every year the factory's management sent the factory's documentation to an external accountant in order to prepare the final accounts. Therefore, the role of the accounting system as a control device in the factory had a limited role in managing and controlling functions (see section 8.4).

Overall, it can be concluded that the role of accounting information in the privatised factories was minimised and the importance of accounting information in the decision-making process was reduced. This was as a result of the state centralisation of some important areas where the accounting information would be used, such as product cost, pricing and budgeting. This finding is congruent with Young (1999, p.161) in his study of East German enterprise when he argued that "Because nearly all decisions of consequence in an East German enterprise were decided by superiors in either the combine of higher planning organs, managers had no incentive to develop accounting information systems." However, in this study, producers in the privatised factories paid more attention to certain accounting information, especially regarding profit calculations, so a large amount of accounting data had to be disclosed to the producers. Thus, there was a change in the importance of the accounting information among producers after becoming owners. This different perception of accounting led to an increase in demand for accounting information on the shop floor. Accounting is becoming more of a distributive mechanism. Bougen (1989, p.225), in respect of the increased demand for accounting information by employees pointed out that "[a]ccounting cost data, selling prices, standard allowances, standard and actual profit margins are some examples of the quantitative, and 'factual' data disclosed to employees." After privatisation, producers increased their demand for accounting information in order to understand the financial situation of their factories and because accounting is the only information source available. Roberts and Scapens (1985, p.451) concluded that "the relative importance of accounting information increases [after privatisation] since it becomes the principal, if not the exclusive bearer of knowledge." Conrad and Sherer (2001, p.530) also concluded that "[a]ccounting information was shown to have taken on a crucial role in relation to organisational change after privatisation."



The accounting systems in the case study organisations produced certain annual accounts such as the income account and balance sheet. Ouibrahim and Scapens (1989, p.16) argued that “the financial accounting system within the enterprise is concerned primarily with the preparation of the annual financial statements for the enterprise as a whole.” These accounts were presented to both internal and external users. Consequently, there was limited actual control during the year. This finding is congruent with Flamholtz’s study where he concluded that “These financial statements (income account and balance sheet) were prepared at the end of each year to determine the firm’s yearly income and financial position both for ownership and tax purposes; but they were not used otherwise in the day-to-day management of business” (Flamholtz, 1983, p.164).

## **9.5 Budgeting system**

In case one, the Head of the Accounting Department made a point of mentioning that from 1988 (the date of privatisation) up until 1995 the Libyan market was stable and most products were sold because of the high demand for them. During this period the management was able to plan so as to meet the demand and determine the supply of the product and set the sales price. The empirical evidence in this study shows that during the period 1988-1995 the Libyan market was closed to all imported products, so that the market was dominated by national products only, without any competition from imports. Thus, it was easier for the factory’s management to prepare its plans and it could more easily determine and influence the national market. In this context, the planning and control function was implemented in the factory in order to achieve the factory’s objectives.

From 1996 up to the date of this research many changes in the Libyan environment have taken place and the ability of the factory’s management to plan and control has become very limited. The production circumstances have changed and the market has been opened to imported products, especially from other Arab countries. National products have faced especially hard competition owing to the shortage of imported raw materials,



spare parts and foreign currency, the latter being influenced by government policy. As a result, there was a perception in the Libyan market that the competition was ‘unfair’<sup>32</sup>. All these circumstances make it difficult for the management of the factory to estimate or predict the market and to make any future plans, thus hindering the management and control function in the factory. It is apparent that the factory is not able to achieve its objectives, especially in terms of production. Indeed, according to the factory’s production reports, it has not achieved its targeted production since 1995 (see Chapter 6). This can be interpreted as follows. Because of the uncertain context of the factory, the control role of the budget becomes very limited and the management prepares operational budgets just to satisfy the state rules and regulations – in order to obtain, for instance, its allocation from the national import budget. Therefore, the budget preparation was not done as a control device in the conventional way but so as to satisfy the state rules. For the Director of Financial and Administrative Affairs “the preparation of the budgets during the present period is useless since there is no possibility of estimating or predicting the cost of the production elements because of the lack of information about those elements and surrounding circumstances ... Therefore, the preparation of the budgets is just being done as a routine and we will stop it [the preparation of the budgets] soon.” Further, there were limited channels for the factory to import the things it needed in terms of raw materials and spare parts and there were only limited sources of foreign currency (the Ministry of Industry and The Central Bank of Libya). Furthermore, the centralisation of the budgeting procedures (allocation, import documentation, exchange rate and customs procedures) had affected the planning and control functions (see section 6.4).

In case two, the Secretary of the People’s Committee also argued that the controlling role of the budgets was very limited because the budgets had no influence on the practical application of the factory’s policies. Consequently, the budgets cannot, for instance, be taken as a substantive basis for controlling and managing the actual activities through serving as a means to identify any divergences between actual and planned activities. The operational budgets were prepared and presented to the Ministry

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<sup>32</sup> In this respect there are trade agreements between Libya and other Arabic countries. According to these agreements Arabic countries have the right to sell their products in the Libyan market but these agreements are abused (see section 6.5).



of Industry for approval, to show the raw materials and spare parts needed and determine the factory's allocation from the import budget. Unfortunately, these budgets did not have any effective control role because they did not reflect the actual situation of the factory's activities. For instance, the figures in these budgets were manipulated and exaggerated in order to obtain a sufficient allocation of foreign currencies (see Chapter 7). The Head of the Accounting Department stated that it was rare that a comparison between the actual budgets and the estimated ones took place. One of the accountants argued that the budgets had lost any effective control role in the conventional sense as a result of a number of factors. Some were related to the state centralisation of the factory's affairs (pricing, budgeting and the import procedures) and others arose from the flotation of the LD against the US\$, when the US\$ became equal to 1.5 LD instead of 0.30 LD. This massive change in the exchange rate led to serious cash problems at a time when there was a lack of an effective banking system to help in solving them (see section 7.5).

The above could be interpreted in the following ways. The budgets were prepared just to satisfy public agencies such as the Ministry of Industry, because it determined the factory's allocation from the state budget. Further, the budgets had lost their conventional control role because they did not reflect the actual situation of the planning function in the factory. Moreover, most of the budget figures were exaggerated in an effort to obtain sufficient foreign currency allocation. Furthermore, the participation of the factory's management in the budget discussion and its allocation was very limited. Consequently, the budget discussion was confined to the personnel of the Ministry and the factory's management had to comply with the outcomes of this discussion.

In case three, the Head of the Accounting Department pointed out that the budgeting system was not applied in the factory except in terms of the operational budget, which consisted of the factory's requirements for spare parts and machinery: this budget was, again, prepared primarily to satisfy public agencies such as the Ministry of Industry. One of the accountants stated that "budgets are done only on paper and are not practically applied. We usually copy the same figures from the previous budget with some minor changes in the figures, but not in the items." Therefore, existing budgets



had not reflected the actual situation of the factory's activities. It appears from the factory's production reports that the shortage of foreign currencies affects the factory's activities in a limited way, because the factory is 100% dependent on local rather than imported raw materials. In TBF the effect of the import budget is only partial, but in the other cases it has a much more significant effect. This finding supported the state aim in the development plan 2001-2005, which encouraged industries dependent on the local raw materials (see section 8.5).

To summarise, four main interpretations of TBF's budgeting system can be put forwarded. First, the budgeting system has only a limited role in managing and controlling the factory's activities as it did not reflect the actual situation in the factory, and on many occasions it was manipulated with a view to gaining sufficient foreign currency allocations. Second, budgets were prepared not for the purposes of control in the conventional sense but as a routine to satisfy certain public parties such as the Ministry of Industry. Third, the informal and personal relationships involved in the budget allocation in the state ministries had an impact on the control function in the factory. Fourth, the limited participation of the factory's personnel in the budget discussion at the Ministry level led to outcomes and allocations that were deemed unsatisfactory. Most of the budgeting outcomes and allocations disappointed the factory's management, as they did not reflect the aims and targets of management.

The findings in this section are congruent with Anderson and Lanen's assertion that "plausible explanation for increased budget accuracy follows from reduced government intervention. In the absence of government intervention, firms have fewer incentives to manipulate budgets and to overspend as a means of altering allocations of government-controlled resources" (1999, pp.396-398). It can be concluded that budgets in the Libyan private organisations have not reflected the actual situation of these organisations but were prepared as a routine to satisfy certain state agencies. This finding is also congruent with that of Hoque and Hopper (1994, p.16) in their study of a Bangladeshi jute mill where they argued that "[a]ccountants sometimes constructed the budget by a 'guess' based on previous years' budgets". Hoque and Hopper (1994, p.18) also go on to argue that "mill managers often overstated their estimates to compensate



for anticipated cuts (in the import budget) to protect their mill in the struggle for resources they returned accounting and budgetary statements routinely in response to (state) orders but made little use of them in the day-to-day management and control of the mill.” Uddin and Hopper (2001, p.654), in their study of a Bangladeshi soap manufacturing company, emphasised that “when preparing budgets, they [accountants] often merely took the previous year’s figures ... with little consideration of actual or likely circumstances.” It also appeared in the cases discussed that the budgets were not linked to the other elements of the MCS so as to achieve the factories’ control objectives. This finding is congruent with Flamholtz’s (1983, p.160) argument that “budgeting is a component of an overall control system and therefore does not actually influence behaviour unless it is linked to other critical components of a control system.” This finding is also once again congruent with that of Uddin and Hopper (2001, p.654) when they concluded that in respect of future uncertainty and state centralisation the “financial budgets became insignificant to operations or for securing accountability.” Therefore, budgeting system in the Libyan private organisations had a limited role in managing and controlling their daily activities and future plans.

## **9.6 Cost and Pricing System**

The Ministry of Economy sets the sales price of the factories products without any consideration of the product cost provided by the factories. By so doing, the sales price was set under the actual cost. This centralisation of pricing and disappointing sales price forced the factories to inflate cost estimates to put upward pressure on prices. Young (1999, p.166) found similar problems in his study of East German enterprise. He argued that “prices for consumer staples were typically set (by the Government) far below costs in order to advance the political objective of ensuring basic economic security for the masses; the prices of some consumer items changed little during thirty years.” Ouibrahim and Scapens (1989, p.17), in their Algerian case study, emphasised that “The absence of cost schedules and price-related documentation at the unit level suggests that accounting information is relatively unimportant.” This is reflected in the Libyan case studies, as summarised below.



In case one, the pricing system was constituted by a number of steps required to determine the final sales prices. The accounting department prepared and calculated the product cost statement in order to send it to the Ministry of Economy as the sales price is determined by it. The total cost of the product contains many taxes, such as the production tax and tariffs not related to the production process but imposed by various public authorities. One of the accountants argued that the Ministry of Industry imposed a production tax of 10% when the factory could not sell any units of its production. As a result, the factory's management could not reduce its product cost in order to compete with imported products. Consequently, cost reduction has only a limited role as a means of control to achieve the factory's objectives, as most of the cost elements are government fees, and these can be changed only by state resolution. This state resolution is unlikely to be issued in the near future as it takes a long series of considerations as a state matter. The Director of Financial and Administrative Affairs noted that "85% of the product cost is income tax, production tax and custom duties. Hence, the factory has no possibility of reducing these burdens without a state resolution" (see Chapter 6). The cost and pricing system in the factory could be interpreted in a number of ways. A lack of skilled accountants, especially in cost accounting, and the centralisation of the pricing decision (the Ministry of Economy) hinder the ability of the factory's management to plan and control its activities; an ignorance of the product cost when determining the sales price in the Ministry of Economy limits the accuracy of the cost calculations in the factory; very high taxes and fees were imposed by the state on the national products. Consequently, the factory management had limited opportunities to implement a cost reduction strategy in order to face new competition in an open economy (see section 6.5).

In case two, the Ministry of Economy is the only authority in the country that has the right to determine the sales price of all national products. As paper products are considered crucial to Libyan society, the Ministry of Economy fixes the sales price of these products without any balanced consideration of the product cost. The factory accounting department prepares a costing schedule for paper products and sends it to the Ministry of Economy to help in the determination of the final sales prices. Yet most of



these cost schedules are not taken into account by the Ministry of Economy. Furthermore, it is very common that the final sales price determined is actually less than the cost of the paper products (see Chapter 7). It can therefore be concluded that the product cost and price have only a very limited role in managing and controlling the factory's day-to-day activities. Therefore, product cost and pricing had a limited role as a control device in the factory (see section 7.6).

The ANF product cost and pricing situation could be interpreted in a number of ways. Owing to a lack of skilled accounting personnel the accounting information, especially in terms of the product cost, was minimal; the factory accountants prepare the product cost, but the use of the product cost in planning and controlling the factory's activities was very limited, because the final decision regarding many of the factory's affairs (pricing and budgeting) is made outside the factory's boundaries (by the state); an ignorance of the real product cost in sales price preparation in the Ministry of Economy greatly limits the impact of any cost calculations by the factory.

In case three, the main source of sales is the finished products, i.e. the bricks. The cost of the product elements is prepared by the accounting department (whose role is completed by achieving the cost calculations). The cost statement is then sent to the Ministry of Economy for approval and calculation of the profit margin in order to identify the sales price. The management of TBF plays a vital role in calculating product cost because most of its production elements are available locally. Consequently, the influence of the management on the cost of raw materials, for instance, is direct as there are many choices of raw materials sources to select from. However, the product cost figures are typically exaggerated before being sent to the Ministry of Economy in order to gain a high profit margin. Analysis of the factory's documents showed that the factory has achieved its profitability objectives (see Chapter 8). The pricing procedures in TBF can be interpreted as follows. The profit margin is determined outside the factory's boundaries (in the Ministry of Economy). Hence, the factory management influence on this margin as a planning and control device was very limited; cost calculations exaggerated with a view to obtaining better profit margins (see section 8.6) cannot be used as a basis for any planning and control process; the lack of



skilled accountants; the lack of understanding of the factory's objectives among the management members and the state intervention in the appointment to posts by appointing unskilled producers all contribute to an increase in the product cost and to difficulties of using costing and pricing information in planning and controlling functions. So, the positive role of accounting information was reduced in these areas.

## **9.7 Clarification of the impact of the key external contextual factors**

Key contextual factors identified by participants as adversely affecting the management control process at the factory level were: state intervention, economic sanctions, political structure and social-cultural relationships. These will be considered below. Otley (1999, p.381) concluded that "there is a need to focus on the external context within which the organisation is set, rather than just being concerned with internal activities." Hoque *et al.* (1994, p.434) argued that "management control in organisations can only be understood through a holistic approach. To limit it to formal bureaucratic systems, thereby ignoring socio-political and cultural aspects, is likely to give a misleading impression leading to erroneous policies."

### **9.7.1 State intervention**

The state plays an important role in managing and controlling the factory's day-to-day affairs by trying to use its relations to influence factory activities and to show that it still controls everything in the country. Indeed, the state intervenes in many aspects of the factory, such as its pricing system, budgeting and the structure of the People's Committee and the Congress Committee. All these functions, according to the official privatisation documents, should be implemented within the factory management system (see Appendix A).

#### **9.7.1.1 The pricing function**

The state centralised the pricing procedures of the factories' products by giving the Ministry of Economy the single right of authority to determine the final sales prices.



The costs of the products are prepared by the factories and sent to the pricing department in the Ministry of Economy to help them in determining the final price but these statements appear often to be ignored and the final price is contrary to the expectations of the factories' management, typically being less than was anticipated (see sections 6.5, 7.5 and 8.6). The state pricing policy is based on the cost of the product plus 10-15% as a profit margin, but as mentioned earlier in sections 6.5, 7.5 and 8.6, this policy has not been either realistic or feasible in the history of the privatised factories, and the sales prices appear to be reached on the basis of the Ministry's own cost, the source of which is unclear, but tend always to be less than the cost as estimated by the factories. Hence, factories sell their products at a loss, since they have no option but to comply with the Ministry of Economy prices. All the factory managers complained that people in the Ministry of Industry took no responsibility for considering and understanding uncertain elements such as the fluctuation in product prices and the exchange rate of the LD against the US\$ (see sections 6.5, 7.6 and 8.6). This is despite their retaining their powers of intervention in the day-to-day affairs of the factories; the centralisation of product pricing is an obvious example of this intervention.

#### **9.7.1.2 The budgeting function**

Personnel in the factories had little or no influence over the budget process and the accountants in the factory prepared operational budgets only because the Ministry of Industry required them to do so. Indeed, most managers and accountants argued that they prepared budgets routinely in response to government orders but made little use of them in the day-to-day management and control of the factories. It was evident that the accountants just altered and edited the previous month's statements to prepare statements and reports due for the current month. No detailed variance analysis by product was done at the factory level, and the budgetary process in the factories had become mechanical, obsessively rule-bound and, in practice, divorced from any substantial operational control (see sections 6.4, 7.5, 8.5 and 9.5).



### 9.7.1.3 The appointment function

The state also intervened in the appointment of the chairperson of the People's Committee and the Congress Committee by encouraging the employees (producers) to elect specific people for these posts in the Productive Congress meeting. According to the written documentation such as the ownership contract, the right of appointing someone to the People's Committee and the Congress Committee lies with the Productive Congress (see Appendix A). Yet it was evident that the state, through its agencies, sent recommendation letters for people in the factory to help them obtain posts in the People's Committee and the Congress Committee. Indeed, on many occasions the state appointed a person from the Ministry of Industry as the chairperson of the People's Committee just to manage and control the factory's day-to-day activities. Specifically, the Secretary of the People's Committee of ANF had been working in this post for 13 years merely because he had been recommended by some people in the state (see sections 6.2, 7.3 and 8.3).

In summary, it is evident that state intervention in the day-to-day processes in the privatised factories played a vital role in hindering the ability of these factories to implement their own policies and plans in order to achieve their goals (see sections 6.4, 7.5 and 8.5). Smallbone and Welter (2001, p.64) stated that "the state is one of the key influences on the external environment in which businesses develop in any economy, acting as enabling and/or a constraining force." This finding is congruent with that of Alam (1997, p.163) in his Bangladeshi case studies where he concluded that "due to the lack of operational freedom and intervention from higher authorities, the spheres for articulating organisational strategies to tackle contextual uncertainties are narrowed". This finding is also in line with that of Morris *et al.* (2002, p.367) in their study of Chinese state-owned enterprises when they stated "While the SOEs in theory had free autonomy over managerial appointments, many of the sample enterprises complained of continued government interference — whether central or local — over appointments." This finding is also congruent with that of Hoque *et al.* (1994, p.430) in their study of a Bangladeshi jute mill when they argued that "Most mill managers complained that the top levels of management in BJMC [Ministry of Industry] took no responsibility for



managing the uncertain environment despite retaining their centralised powers to intervene in the day-to-day affairs of the mill.” Thus, people in the Libyan privatised factories have little or no influence in many day-to-day functions such as pricing and budgeting.

### **9.7.2 Economic factors**

Economic factors, including policies and regulations, notably including tax laws, commercial agreements, economic sanctions and lack of foreign currencies and the international oil prices all affected the management control functions in the factories in a number of ways. All privatised factories had to submit their production requirements to the Ministry of Industry in the form of an import budget. This budget contained the required raw materials and spare parts needed to achieve the targeted production. The content of the import budget was used to determine the share of foreign currency the factories received in the state import budget. Unfortunately, according to this study, it is clear that the factories typically receive only small allocations of foreign currency, much less than the actual amount required. This shortage in imported production components led to a failure to achieve the targeted production in the privatised factories. Research investigation revealed that during the period 2000 to 2002 the three privatised factories constituting the case studies received less than 50% of their requirements (see Table 9.3). This was because people in the Ministry of Industry appear not to have studied the actual requirements of the factories. This shortage in the allocation of foreign currencies has engendered low production levels and significant losses in recent years (see Table 9.3).

Another factor that affected the factories’ activities was the drop in international oil prices. This affected the whole industrial sector because of the Libyan economy’s dependence on oil revenue for all its development plans. The contribution of industrial exports to the total exports of Libya during the period 1987-1996 was very low because much of the exported production was constituted by crude oil (see Chapter 5).



Table 9.3: Allocations of foreign currency to the factories from the state budget.<sup>33</sup>

The factory	Year	The factory's estimated requirements (LD)	The factory's allocation (LD)	Allocation as % of factory requirements
LFFF	2002	6,648,340	900,000	13%
ANF	2000	20,415,888	1,530,000	8%
	2001	20,415,888	1,050,000	5%
	2002	8,859,601	Zero	Zero
TBF	2000	650,000	273,000	42%

Source: The Ministry of Industry report, Tripoli, 2002.

Table 9.4: Summary of national revenues and expenditures of Libya (Million LD).

Items	Year			
	1998	1999	2000	2001
1) Revenues:				
• Oil revenues	2,551.0	3,444.4	2,203.0	3,603.0
• Non-oil revenues	1,815.0	1,412.6	2,459.2	2,395.8
Total revenues	4,366.0	4,857.0	4,662.2	5,998.8
2) Expenditures:				
• Administrative expenditures	3,163.8	2,966.9	3,153.2	3,596.6
• Development expenditures	485.2	794.1	1,541.0	1,539.0
• Extra budget	792.0	535.0	556.0	496.0
Total Expenditures	4,441.0	4,296.0	5,250.2	5,631.6
Net (+/-)*	(-)	(-)	(-)	(+)

Source: The Central Bank of Libya Bulletin, first quarter, 2003.

\* Presents the sign of the sum of 1-2.

<sup>33</sup> There was a shortage of data regarding LFF and TBF, but it was possible to determine that they received small allocations over the period.



The drop in international oil prices during the last decade had a negative impact on the Libyan economy in general and on the industrial sectors in particular. Hence, many development plans were delayed (see Table 9.4). The oil price collapse engendered serious cash flow problems and had adverse consequences for the economy. This was compounded by the economic sanctions imposed on Libya in 1990 by the US and UN. The restrictions on the movement of individuals, products, spare parts and raw materials negatively influenced forward investment and innovation. Furthermore, the sanctions affected day-to-day processes in the Libyan economy. This negative impact was apparent in terms of low productivity and quality, shortage of raw materials, spare parts and foreign currency, old technology, limited experience and the absence of training programmes.

#### **9.7.2.1 Financial market and banking policies**

After the development plan of 1973, the public sector was the dominant force in the Libyan economy and it was supported by the financing of the whole of the country's activities from oil revenues. As a result of the oil price collapse in the 1980s, the public sector faced serious financial and management problems (low revenues and a huge number of employees) and this pushed the Libyan decision-makers to pay more attention to the improvement of the private sector rather than the restructuring of the public sector. In the late 1980s, a group of public organisations had ownership transferred to the private sector (see Chapter 5). As a result, the private sector now plays a vital role in the Libyan market (The Central Bank of Libya periodical, December, 2002, pp.5-6). According to The Central Bank of Libya periodical, the advantages of having Libyan stock and financial market are as follows:

- to improve the role of banks in financing the private organisations by providing long-term and medium-term loans to develop their activities;
- to expand the base of private ownership, which is the state target of privatisation;
- to simplify the process of transferring the public ownership to the private one;
- to facilitate the circulation of the private and public organisations' shares in order to increase or decrease their capital;



- to give opportunities to private organisations to choose their own finance methods and reduce state intervention in their activities.

To recapitulate, up to the time of this research there have been proposals – and only proposals – for setting up Libyan stock and financial markets. The view is that the lack of any Libyan financial market has led to a high degree of uncertainty in market circumstances. The Libyan economy will continue to struggle to overcome many financial, management and control problems. Indeed, the privatised factories are struggling to identify achievable objectives. This is illustrated by the fact that the three cases in this study were all suffering from a lack information sources for decision-making, which put a pressure on accounting in the context of privatised factories.

### 9.7.3 Political interference by state agencies

The clearest political influence is evident in the type of structure in the factories. According to the state political system, the structure and management of all entities in the country, even private ones, must be constituted by management and controlled by the People's Committee and Congress Committee (see Chapter 4). It is prohibited for an individual alone to own any factory or company in Libya, and this imposed structure affects the management's ability to manage and control the factories' activities. This is because the committee members rarely agree about how to develop and improve plans and strategies. The state agencies' vision regarding the privatised factories also affects the management and control function in these factories because officials in the public sector see the private sector as a competitor, and not as an integrated part of the country's economy. This is in evident in the allocation of the foreign currency budget. It appears from Table 9.5 that public companies got what they needed from the foreign currency budget, whereas the privatised factories received about 60% of their needs.

Table 9.5: The foreign currency budget in 2001.

Sector	The requested US\$	Actual allocation US\$	%
Public companies	41,000,000	41,000,000	100%
Privatised factories	16,320,000	9,700,000	59%

Source: Ministry of Industry, Tripoli Municipality, 2002.



#### **9.7.4 The influence of personal and informal relationships in the context of private companies**

In addition to the influence of the state in the structure and organisation of the factories, it is clear that personal and social relationships play an important role in their day-to-day processes. Appointment to posts in the factories do not appear to be based on any specification or experience. Indeed, the Head of the Accounting Department in TBF said that:

“The Productive Congress decided to replace the sales manager. This was done purely on consideration of personal and social relationships. In addition, this person wanted to be not only the sales manager, but also to be the production manager, even though he has no experience. Thus this person, without any apparent background in production, is there only on account of whom he knows, not what he knows”.

A serious situation exists with regard to the election of the People's Committee and the Congress Committee in the factories. Most of the elected people have a low level of education and little experience of financial and administrative matters. Consequently, their poor awareness and understanding of financial and administrative affairs has a negative impact on all the activities of the factories. One member of the People's Committee stated that “in the first meeting of the Productive Congress in this factory, the Congress Committee was composed of 5 members. At least 4 members can not read or write.” To give a clear picture of the lack of experience and education among elected people, according to the research investigations, it was evident that most of the Congress Committee members have low awareness regarding the expenses and revenues of the factories. This low educational level and lack of experience among the producers causes many problems in the factory and make it difficult for the management to persuade the producers to implement any changes or developments in the factories' systems.



The second serious problem in the factories was the number of surplus employees on the shop floor. Most of those employees had been employed by the Ministry of Industry without any consideration of the factories' needs. They had no jobs to do, and either just stayed in the departments, or, on many occasions, hindered or interrupted the production processes because they believed that no one in the factories could punish or dismiss them. The Production Manager in TBF noted that there were more than 10 employees in the department without any real jobs to do and they were unskilled people. Consequently, it was difficult to incorporate them in the production process and they remained in the factory only because they had relatives in the Ministry of Industry. According to the field observations, one employee in the production department was entering the office of the Secretary of the People's Committee many times a day without following the administrative routine and formal procedures in the factory (e.g. obtaining permission to enter the Secretary's office). This happened because he had some relatives and good personal relations in the Ministry of Industry. Most of the important posts in privatised factories are (formally or informally) controlled by the Ministry of Industry. This is in direct contradiction to the official written documentation such as the ownership contract (see Appendix A).

One of the important cultural factors affecting the factories was the Islamic religion, as interest on loans is prohibited in Islam. This prohibition led to most Libyan producers boycotting bank loans. Finding alternative means of finance was very difficult for the privatised factories, especially with a lack of Islamic banks. As a result, the management delayed many plans and activities from a lack of financial sources (see Chapter 4).

In conclusion, it is apparent that employment procedures and other cultural factors are adversely affecting the ability of management to manage and control the day-to-day activities of their factories. This finding is congruent with that of Hoque and Hopper (1994) in their study of a Bangladeshi jute mill when they argued that the mill managers used a variety of social and informal control mechanisms to cope with the contextual uncertainty. According to the research investigations, the managers of the privatised factories have drawn from their informal and personal relationships to obtain allocations



from the state import budget greater than they would have otherwise got (even if still insufficient) and to speed the process of the administrative procedures in the Central Bank of Libya (see sections 6.4, 7.5 and 8.5).

## **9.8 Overview of chapter**

This chapter provided an overview of the three case studies conducted for this research study. The similarities and differences between the MCSs in each factory were studied. The environmental factors that influence and shape the actual situation of MCSs in the Libyan private sector were discussed and analysed. Notably, most of the MCSs in the three cases were similar, a similarity that might be attributed to the similar environment that these factories were in. All the case studies were affected by the environmental circumstances surrounding them. This chapter was divided into two parts. The first part dealt with the existing MCSs in the three case studies. The factories' objectives were discussed across the cases and it was found that a misunderstanding of the factories' profit objectives among the producers had led to difficulty for the People's Committees in managing and controlling the factories' activities. The factories' management and structures were studied and similar formal structures were found in all the cases. This was understandable as these structures had been imposed by the government. In contrast, however, the relations between the structural parts were different according to the individuals and context involved. The accounting information system, the budgeting system and the cost and pricing system were discussed across the three cases in order to identify similarities and differences among these cases.

The second part of this chapter addressed the impact of the contextual factors on the MCSs found in the privatised factories. State intervention was a significant external factor that had influenced the shape of MCSs in the privatised factories in terms of budgeting, pricing and appointment functions. Economic factors such as the UN and US economic sanctions had affected the day-to-day activities in privatised factories and clearly hindered the management and control process. Political influence was also apparent in terms of the management and structure of the privatised factories and the social and cultural relations also had a great impact on the MCSs in the factories,



especially in terms of appointments, People's and Congress Committees' elections and decision-making processes.

It can be concluded that contextual factors play an important role in shaping MCSs in these Libyan private organisations. This finding is supported by many studies emphasising the importance of and the impact of environment on organisations (Lowe, 1972; Lowe and Tinker, 1979; Lowe and Chua, 1983; Otley, 1985; Lowe and Puxty, 1989; Hoque and Hopper, 1994; Hassard and Sheehan, 2002; Wickramasinghe *et al.* 2004). The next chapter provides an overview of the research findings, research limitations and discusses new avenues for further research.



## **Chapter 10: Summary and Conclusions**

### **10.0 Overview of the research approach**

The selection of the interpretive perspective here (see Burrell and Morgan, 1979; Hopper and Powell, 1985; Chua, 1986; Laughlin, 1995) was made in accordance with the researcher's beliefs and the nature of the research topic. The researcher's emphasis is that social reality is subjective. Knowledge of the social world is subjective and acquired through personal experience. The researcher's main objective was to explore and understand the phenomenon of MCSs in a small number of Libyan private organisations (case studies) in a particular transition context. The interpretive approach used here aims to understand reality substantially from the participants' point of view. The exploratory and explanatory nature of the study was one of the reasons for adopting a qualitative approach (Creswell, 1994).

Only a few previous studies have been concerned with management control in the Libyan environment. All studies to date have focused on Libyan state-owned companies and virtually no attention in these studies has been given to private sector companies. There has also been limited emphasis given to the on-going transition context of Libya in this regard, a context involving change of organisational ownership towards 'privatisation'. Little focus has been given to the "social processes whereby such systems are implemented ... or how they come to be used in the way they are" (Brignall and Modell, 2000, p.282). This research project adopted a qualitative approach with a view to understanding MCSs in their 'natural' setting (Tomkins and Groves, 1983). Many studies have supported a qualitative approach as a way to expand knowledge of business practices in the real, everyday context (Tomkins and Groves, 1983; Hopper and Powell, 1985). The researcher placed "[no] emphasis on mathematical analyses, statistical tests, surveys and laboratory tests ... [but] more on studying how practitioners perceive their worlds, what issues concern them, why these issues concern them and how they perceive them affecting accounting practices and the influence accounting



has” (Tomkins and Groves, 1983, p.364). A case studies approach was adopted in order to gain rich descriptions of actual situations of MCSs and a better understanding of the context and factors shaping and influencing these systems (Kaplan, 1986; Parker, 1994). The case study involved multiple sources of data (interviews, document analysis and observations) to achieve validity and reliability (Yin, 1994, 2003).

Systems ideas were used in this research in order to direct attention to various functions in the context of an interpretive approach, with the aim of contributing to a holistic understanding of management control functions in the Libyan private sector. Systems ideas were also helpful in shaping a better understanding of the environmental factors that influenced MCSs in the Libyan private organisations studied. For Otley (1983), the use of systems ideas in studying MCSs helps in understanding an organisation as one system instead of considering its parts as isolated components. Thus, there was a conscious attempt to be holistic rather than reductionist in approach.

## **10.1 An overview of the Libyan privatisation experiment**

The objectives of the privatisation experiment to transform Libyan public sector organisations were regarded by the state to be themselves a vital part of the privatisation process (Ministry of Industry, 2000). To appreciate these, some contextual insights have been shown to be important. First, an increase in oil prices since the beginning of the 1970s until the mid 1980s led to a surplus of finance for the Libyan government. This surplus was and is used to support socio-economic development programmes. Second, the aims of these programmes were to diversify revenues and limit the dependence on oil, to create a productive, industrial base and to procure the necessary infrastructure to achieve economic growth. Third, it is clear that during this period the national economy was dominated by the public sector, which had become the main source of investment. However, in the mid 1980s and with oil prices starting to fall, the national economy suffered from several difficulties such as an imbalance in the public budget and balance of payments problems (Ministry of Industry, 2000). The decline in the performance of public sector companies also played a key role in exacerbating such problems. State-owned companies were deemed not sufficiently competitive and were incapable of



substituting for oil as the main source of income in the Libyan economy. Their competitive capacity was extremely low and aggravated the deterioration of the balance of trade. Furthermore, public sector enterprises registered constant losses and needed continuing support, which deepened the financial deficit. Accordingly, economic growth, investment and business administrative performance had declined. These environmental influences helped constitute the object of rebuilding and reforming the structure of the national economy and giving the private sector a larger opportunity to contribute to the national economy.

## **10.2 Characteristics and features of the Libyan privatisation experiment**

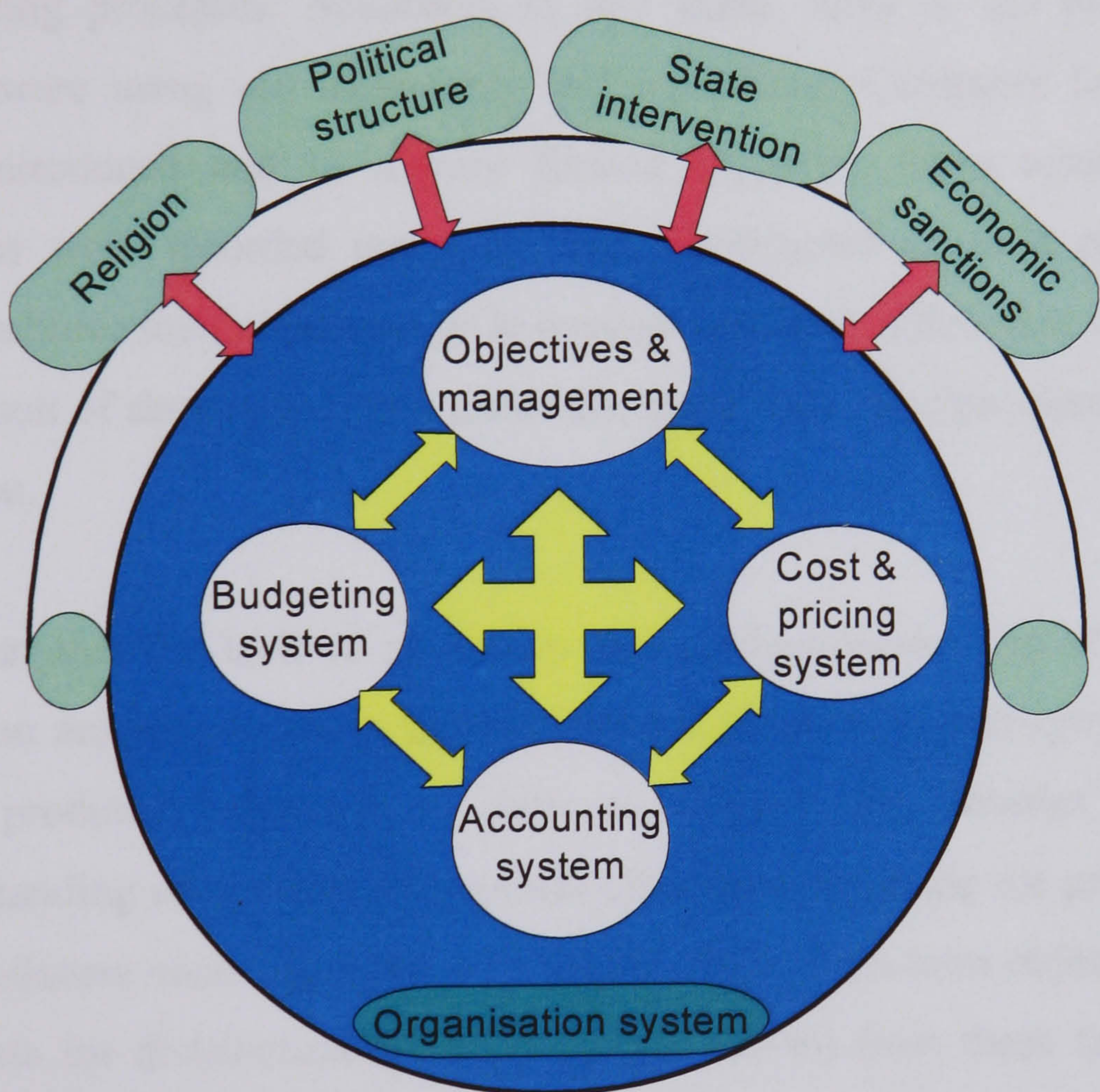
1. It is clear that the privatisation method adopted in Libya has not primarily distinguished between the employees and management. The empirical evidence of this research showed that there was ambiguity in the internal rules and regulations regarding the rights and duties of the management and producers. This situation led to conflicting interpretations of these rules. For instance, every producer wants to be an active member in the factory's management (see Chapters 6, 7 and 8).
2. Despite significant difficulties in the privatisation process, it is being speeded up without fully understanding the socio-economic and political consequences of this process. Furthermore, the privatisation process has developed rapidly and been implemented in Libyan society with a lack of appropriate attention to the legal and economic infrastructure.
3. The privatisation was achieved by selling state-owned factories to the employees. The General Committee of privatisation used the book value of the factories' assets to calculate the final sale price for these factories. The present study has revealed that using the book value in the privatisation process was misguided because the actual value of some of these factories was almost zero. Therefore valuation of the factories using this questionable method has arguably been unfair as some employees have acquired valuable companies, whereas others have not.



4. Accounting procedures and standards were not specified or even mentioned in the ownership contract of the privatised factories.

### 10.3 The research findings

The research findings emerged from the interactions and development between the theoretical framework in Chapter 1 and the empirical investigations, as shown in Figure 10.1.



**Figure 10.1: The actual context of the MCSs.**



With regard to organisational objectives, it was found that the lack of skilled personnel in privatised factories and the lack of training programmes for the employees led to misunderstandings of the objectives of the privatisation process. Further, the misunderstanding of the factories and state objectives encouraged the employees to think that they were the owners and that nobody could impose rules or regulations upon them. According to the case study explorations, this misunderstanding hindered the factories' management in respect of achieving planning and control of their activities. It was also very worrying that there was a lack of technology in production processes and in accounting processes. According to this study, most of the privatised factories' machines were using old technology and equipment. Computer facilities were only recently introduced and in a very limited capacity. As a result, all accounting transactions were recorded manually. This contributed to most privatised factories failing to achieve their objectives or to manage and control their day-to-day affairs. This was the result of shortages of raw materials, spare parts, foreign currency and high state intervention.

It was clear that the lack of awareness and a misunderstanding of the objectives of privatisation among producers led to serious difficulties in managing, controlling and orienting producer behaviour in order to achieve the factories' objectives. This misunderstanding of the state's long-term objectives regarding the privatisation process among producers encouraged them to achieve their short-term objectives by obtaining benefits (via the distribution of profits to themselves) from these factories as soon as they could. All the above factors led to an increasing loss of trust among producers in state policies and regulations regarding the privatisation process. Producers tried to distribute all the profits of the factory instead of capitalising them in order to improve and develop their factory. This study revealed that most producers mentioned the example of the Al-Afia clinic, which was privatised in the past, but the state then re-nationalised it. This evidence made producers expect the same action in respect of their factories. This led to the factories' management being unable to plan, control or influence personnel in order to achieve the targeted objectives. Pressure was put on the accountants to prepare and provide the final accounts on time as producers wanted to



view accounting information because they wanted to see how much profit has made and what their allocation of this might be (see sections 6.1, 7.2, 8.1 and 9.1).

With regard to the organisational structure and management, the study has shown that there is an ambiguity in the responsibilities in the privatised factories and unclear relationships between the factories' subsystems and between the factory system and external agencies such as the Ministry of Industry. According to the case studies, the organisational structure seems to be simple but it is actually very complex as a result of a lack of clear-cut relationships. The written documentation, such as the ownership contract, shows that general responsibility lies with the People's and Congress Committees, but in practice the Secretary of the People's Committee has all the rights to manage and control the factory without any accountability to the Congress Committee. This ambiguity of responsibilities and duties led to an increase in the role of informal relationships in managing and controlling day-to-day activities. This kind of change in the management and ownership structure is a unique feature of the Libyan context; it was difficult to locate much literature in these areas. As a result of the lack of previous studies, these areas need more empirical research in order to gain a richer understanding of the actual situation of the phenomenon under investigation.

With regard to organisational management, the empirical evidence reveals a lack of any formal basis for the selection of the factories' management teams. From the case studies, it was found that experience and educational level played no role in the selection of the management. Most of the management had a very low level of experience and education. This situation affected the decision-making process in the privatised factories. Given the lack of skilled personnel who plan and control their activities, the planning function almost disappeared from these factories. Furthermore, there manifested a conflict and contradiction between the official privatisation documents and the actual management situation in the factory. The official documents suggested that these factories should be managed and controlled independently and in a private way in most of their daily affairs. In practice, the Ministry of Industry still controls much in the factory, and people in the Ministry behave as if the factory is still state-owned. This leads to great state influence on the management and forces it to



orient all its policies, reports and budgets to satisfy the state agencies (see sections 6.2, 7.3, 8.3 and 9.3).

With regard to the accounting system, the empirical evidence shows a lack of accounting standards and quality accounting in the privatised factories. No unified and consistent accounting system is in place to serve all private sector companies. All the accounting departments in these factories relied on the ability and education of their accountants, who tried to implement what they had studied at university without reference to any general accounting standards. As a result, the accounting applications were likely to differ from one factory to another. The shortage of good quality and unified accounting rules led to a lack of useful accounting information provided to decision-makers in these factories, which directly affected the planning and control functions in these factories.

The research investigations show that the Ministry of Industry's involvement in the day-to-day affairs of the factories, such as in budgeting and pricing policies, led to a minimisation of the role of the accounting information as an information source in the factories and a reduction in the importance of the accounting information in these areas. Personnel in the factory did not pay attention, for instance, to cost information because the sales prices were determined by the Ministry of Economy.

The empirical evidence also revealed that most of the privatised factories did not prepare any financial reports to reflect their economic and financial situation. From interviews and document analysis, it was apparent that no financial reports had been prepared except the final accounts, such as the income statement and the balance sheet. These accounts were requested by the state and the producers in order to ascertain their profit allocations. This lack of financial reporting for management affected the management's ability to obtain the necessary accounting information in good time in order to manage and control the day-to-day activities. As a result, little or no feedback process existed in these factories. In addition, the lack of skilled personnel, especially in accounting departments, left the accountants mere record-keepers. This limits the role of the accounting system to a mere recording process instead of a means of providing



accounting information for the decision-makers to help them in managing and controlling their factories.

Important issues in the privatisation process were income distribution and the profit calculations. The general idea of the Libyan privatisation experiment was to distribute the profit equally among producers. Yet the profit calculations were implemented differently in privatised factories. Two different methods were used to calculate the producers' salaries in order to calculate the profit: the points method and the state Salaries Law No.15 of 1981. Because of this change of thought about profit, the role of the accounting information was altered<sup>34</sup> and much of the accounting information (for instance, turnover and expenses) was used to calculate net profits.

As a result of the change in the role of the accounting information, there was a change in the producers' perspective upon accounting information, especially in respect of revenues and expenses. After privatisation, producers paid more attention to the accounting information and the final accounts. They asked for explanations of all the figures in the final accounts. It was not just the role of accounting information that changed but also the users of this information (see sections 6.3, 7.4, 8.4 and 9.4).

With regard to budgeting and planning systems, the case study investigations revealed that budget preparation was very limited as a result of the state-led centralisation of the budget allocation. This centralisation led to preparing the budgets merely as a routine to satisfy the state agencies such as the Ministry of Industry and in order to attain a sufficient allocation from the import budget. Consequently, the role of accounting became limited and seems to be less important *vis-à-vis* its ostensible objective as budgets did not reflect the actual situation. Also as a result, because of the decisions regarding the budget allocation made at the Ministry of Industry, people in the factories may distort the information in these budgets. The decisions at the top, which are based on distorted information, can be misguided. People in the factories are required to follow the higher level decisions so they do not use available information for managing and controlling their affairs.

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<sup>34</sup> Before the privatisation process, the Salaries Law No.15 of 1981 was the only method implemented.



It was found in the case studies that the lack of foreign currency for importing the production needs, such as raw materials and spare parts, led to the low productivity of privatised factories. This study revealed that as a result of shortage in raw materials and spare parts, none of these factories achieved its targeted production. This finding affected the budgeting system in these factories, as managers were unable to predict and estimate future circumstances. No budgets were prepared except the operational budget, which was prepared to satisfy the public agencies and state rules. Thus, budgeting lost its important role of managing, controlling and motivating the personnel to achieve the factories' objectives (see sections 6.4, 7.5, 8.5 and 9.5).

With regard to cost and pricing systems, the present study has shown that cost information seems to be considered to be 'relatively unimportant'. There were no cost sections in the privatised factories and product cost was prepared by a general accountant. This general accountant has limited accounting skills to provide the decision-makers with sufficient information. Consequently, the usage of accounting and cost accounting information in managing and controlling functions was very limited. This cost preparation was not taken into account when the Ministry of Economy determined the sales prices. Thus, pricing had a limited role in managing and controlling activities and was not an important task because it was done externally (at the Ministry of Economy). The centralisation of the pricing process at the Ministry of Economy decreased the management's motivation to improve and develop their cost accounting practices. This study revealed that the privatised factories used to prepare product cost twice a year and sent it to the Ministry of Economy. This cost preparation was not taken into account in determining the final sales price. On many occasions, the sales price was determined at less than the cost of the product. Centralisation had a negative impact on the privatised factories, hindered the management to plan and control its future and led to their failure to achieve their objectives. Furthermore, the role of accounting information in these important areas was minimised as it was not taken into account in the decision-making process (see sections 6.5, 7.6, 8.6 and 9.6).



With reference to the impact of environmental factors on MCSs, the present study indicates that contextual factors played a very significant role. State intervention, economic sanctions and agreements, the political structure, culture and employment factors all contributed to shaping and influencing the existing MCSs in the Libyan private organisations. As a result of the absence of Libyan stock and financial markets, accounting (or those who might provide it) was under pressure to provide the necessary information for producers and all other users (see section 9.7).

Ultimately, it could be argued that the findings of this study provide a powerful contrast to the expectations of Western management accounting. According to conventional Western wisdom, the management accounting and control function of a company is expected to develop and use effective accounting systems, which provide useful information for the management of the organisation. This accounting information helps the decision-makers to manage and control their activities effectively, through the accounting system, which provides up to date financial reports reflecting the actual situation of the organisation. Budgeting systems and cost calculations are held to play a vital role in the planning and control function in organisations and are considered as an important means of motivation in order to achieve the desired goals. Companies frequently adopt one or two basic types of costing system to assign costs to products or services (job-costing systems or/and process-costing systems). Consequently, costing systems aim to report cost numbers that reflect the way chosen cost objects use the resources of an organisation. For instance, cost-volume-profit relationships or activity-based costing can assist managers in understanding the behaviour of total costs, profit and selling price. Cost calculations may also be used to determine the final sales prices. The cost-plus pricing system, for example, chooses prospective prices by using a general formula that adds a mark-up to a cost base. Thus, management accounting and control systems are held to form an integral part of the structure and functioning of business organisations.

One of the most revealing aspects of this study is that most of the above expectations about the nature and purposes of management accounting do not apply to Libyan privatised companies. Accounting systems in these companies provide very limited



accounting information and the usage of this information in the planning and control process was also very limited. No financial reports are prepared except the annual statements (income account and balance sheet). These statements did not reflect the actual situation of the organisation's activities, but were distorted in order to achieve maximum allocation of resources from the ministries. Budgets are used just as a routine to satisfy the state ministries in order to gain sufficient allocations from the state budget. Therefore, budget preparation was not done as a planning and control device in the conventional way. Also, costing systems of the type described above do not exist and cost calculations are not taken into account when determining the final sales price, as the latter is determined externally at the Ministry of Economy. With no control over pricing and limited control over costs much of the need for 'conventional' styles of management accounting information does not exist. As a result of the unique context of Libyan privatised companies the form and function of accounting has been shown as entirely different to that which the reader of an accounting textbook would have expected.

#### **10.4 The link between the main findings and the literature**

This study's findings reveal that environmental factors have had a significant role in shaping the actual situation of MCSs in the Libyan private sector. These findings have supported aspects of previous studies and arguments in the literature. Lowe (1972), Lowe and Tinker (1979), Lowe and Chua (1983), Otley (1985), Lowe and Puxty (1989), Hoque and Hopper (1994), Hassard and Sheehan (2002) and Wickramasinghe *et al.* (2004) argued that the environment has a vital role in an organisation's day-to-day life and that an organisation survives when there is a need for it in the environment. However, this study's findings found the conventional approach of management control inappropriate, as it narrows the scope of management control and restricts its possibilities (see Chapter 3).

The empirical investigations indicated that the focal factories had not achieved their planned objectives. This failure resulted from the management of these factories losing one of the most important means of control in the factories. Lowe (1972), Lowe and



Chua (1983), Otley (1985) and Chua (1986) argued that organisational objectives are important devices to guide and orient personnel in an organisation. The present study showed that the formal structure of the privatised factories was imposed externally by the state, so this structure was not the choice of the factories and has not reflected the administrative and control needs in the factories. This situation led to misunderstanding among personnel in respect of managing and controlling functions (see Chapters 6, 7, 8 and 9). This finding is in line with studies of Uddin and Hopper (2001) and Flamholtz (1983). This research also suggested that the role of accounting information in managing and controlling the privatised factories' activities was very limited because of a range of factors such as the unskilled personnel and the form of state intervention. However, the empirical evidence showed an increased demand for accounting information, with emphasis on profit figures, from producers (Conrad and Sherer, 2001). This high demand for information, coupled to a lack of alternative information sources other than accounting, put pressure on accounting to change and develop its function in order to meet the new circumstances.

Product cost also had a very limited implementation in the factories' decision-making process especially given the way the product pricing function was carried out externally (in the Ministry of Economy). Many studies in different contexts have indicated similar findings, for instance, Flamholtz (1983), Roberts and Scapens (1985), Bougen (1989), Hoque and Hopper (1994), Kloot (1997) and Young (1999). The present study also revealed that budgets had an extremely limited role in managing and controlling the factories' activities and that the influence of the factories' personnel on state budget preparation was also very limited. This situation was a result of state centralisation of budget allocations combined with relative ignorance of the factories' production needs. Any budgets were prepared as a routine to satisfy the public agencies rather than to reflect the actual situation of the factories' activities (Flamholtz, 1983; Hoque and Hopper, 1994; Anderson and Lanen, 1999; Uddin and Hopper, 2001).



## **10.5 The link between the main findings and the research methodology**

The interpretive approach was adopted in this study in order to attain ‘closeness’ to the people in the focal organisations and to understand the current situation of the MCSs from their words, opinions and experience. The interpretive approach was appropriate given the concern to capture the richness of the task of understanding. It facilitated the researcher’s understanding of the practices of MC adopted by people and how and why they did so adopt. A combination of the interpretive approach and systems ideas was useful for gaining a better understanding of the MCSs in the private organisations and their relationships with their environment. This combination was helpful in achieving the research objectives and providing an in-depth understanding of the MCSs in the Libyan private sector. Using multiple data collection methods was deemed appropriate in order to capture detailed data regarding MCSs and to give the researcher the opportunity to understand the existing and changing MCSs more clearly because of the direct contact with participants involved.

## **10.6 The contribution of the study**

1. The study contributes to the limited studies on MCSs in developing countries in general and within the Libyan context in particular (see Chapter 3), although generalisation from this study’s findings was not the aim of this researcher. This study provided a wider and deeper understanding of the MCSs and the influence of the social, cultural, economic and political context on shaping these subsystems in the Libyan private sector.
2. The study reinforced the assertion of prior studies, which indicated the importance of the organisations’ environment.
3. The study contributed to the management control literature, which was considered even today to be widely developed in the theoretical respect but very little developed through detailed case studies (see Laughlin, 1990). The richness and



detail of the data collected reflected and supported the importance of adopting the case study approach when conducting research (Hopwood, 1983; Kaplan, 1986).

4. This thesis contributed to the author's understanding of the relationship between the organisation's subsystems and its environmental factors.
5. This study contributed to our understanding of the actual situation of accounting systems in transition. This research is the first attempt known to this author to explore and understand accounting in transition in the Libyan context.

## **10.7 The study's limitations**

This research has, as with any research, some limitations. These are elaborated upon below:

1. The case studies focused on three private industrial sectors — Food, Paper and Construction Materials. By including further industrial sectors, one might gain wider understanding.
2. The use of three cases in this research was a small sample, which did not permit statistical generalisation to the population of the Libyan private sector as a whole. Nevertheless, the study could be expanded and this is hardly a weakness of this particular study given its specific concern to focus on a few organisations to obtain more detail and richer insights.
3. One of the problematic dimensions of case studies is the researcher's lack of openness to the possibilities of the data because of prior emphatic biases, matters impacting in the collection of data, given the direct interaction with participants and the closeness to the situation. In order to limit this problem, the researcher took a number of steps in the research field (see section 2.3.2.1) and used multiple sources of data, namely interviews, document analysis and observation from three different case studies.
4. In any research there are resource limitations, including time. In one sense this can be considered a problem in any research (Pettigrew, 1990).
5. The lack of a single library for the Libyan industrial sector hindered this researcher in finding much regarding the history of the Libyan industries. The



researcher reinforced the search by exploring personal sources for documents and studies and this was also time consuming.

## **10.8 General recommendations for the focal context**

An attempt can be made here to indicate briefly some recommendations that may be taken to follow from the study.

1. The lack of appreciation by people on the shop floor of how important the role of the management and the decision-making is in the privatised factories led to considerable tension. In order to alleviate this situation, it is recommended that training programmes be established for the producers as a whole with the aim of improving understanding and appreciation of the role of management.
2. The study's findings indicated a deficiency in the range of accounting information submitted to the decision-makers in the privatised factories, owing to the fact that such information, for instance cost information – was prepared by general accountants rather than specialist accountants. Meanwhile, there is an increased demand for accounting information as a result of the growing importance of such information for producers after the privatisation process. It is recommended that further training be established for accountants with insufficient ability in order to improve their performance against nationally accepted standards. This would contribute to the alleviation of this problem as specifically understood here.
3. The study showed a lack of financial report preparation, which led to tension between the accountants and producers in the privatised factories. According to the research observations, most producers went to the accounting department during working hours to ask about their financial situation. It is recommended that financial reports should be published regularly to keep producers up to date with relevant matters, for instance profit allocations.
4. The empirical evidence revealed the limited role of the factory management and personnel in the state budget preparation. This limited participation led to budgets being routinely prepared that did not reflect the actual situation of the privatised factories. It is recommended that the factories' budgets should be initiated by the



factories' management and personnel and reflect the national policy guidelines. With positive participation in key stages of the budget, privatised factories are given a vital motivation to achieve their goals, and budgets will become a more reliable means of planning and control of future activities.

5. It is apparent that the taxes and customs burden imposed on the privatised factories restricted their ability to cope and compete effectively with other products, particularly imported products. It therefore is suggested that the state should reconsider the imposition of such relatively unfair demands and devise a fairer system, which reflects the actual needs and abilities of these factories particularly in the transitional phase of privatisation (until the privatisation experiment establishes itself).
6. Computer facilities need to be introduced into industrial factories to improve product quality and to provide information and final accounts on time. According to this research, it appeared that computer facilities have only been recently introduced into the privatised factories and usage is very limited.

## **10.9 Avenues for future research**

This research study was an addition not only to the growing body of case study research studies in the social sciences but also to the very few studies of management accounting and control in private sector organisations. In addition, it is a first attempt to explore and understand MCSs in the Libyan private companies within their developmental context. Further, this research study has provided experience from which the following avenues for future research can be suggested.

1. This research study revealed that in form at least, if not in effect, little change has occurred in the MCSs in the Libyan privatised organisations commensurate with the change in their ownership statue. Further intensive case studies to investigate the reasons for this resistance to change are recommended.
2. The present study was limited to only three industrial sectors (Food, Paper and Construction Materials) in the Libyan context. Similar studies could be undertaken in the future to explore and understand the MCSs in different sectors.



The findings of this study and similar future studies could be compared to attain a more holistic understanding of the phenomena under investigation.

3. Very little empirical research has considered the Libyan management and accounting systems in transition and development. There is a need for future research to provide a broad overview of the Libyan development plans and policies regarding the privatisation process. The findings of this research and of the future studies could aid the development of state plans and policies.
4. This study revealed the importance of contextual factors in shaping and influencing the existing MCSs in the Libyan private sector. These factors included the UN and US economic sanctions. It is internationally agreed that in the near future these sanctions will be lifted, so there is a need for future research to explore the impact of this change in the external environment on accounting and control functions in the Libyan context.
5. The study revealed that the importance of budgets to the management of the companies appeared to be deteriorating. This may have reflected the nature of budgetary responsibility in the Libyan context, with budgets produced as a quasi-reporting mechanism to the state ministries. Further research could be conducted on this relationship.
6. Despite the often fragmented and undeveloped nature of accounting information in the factories, the accountants retained a high status within these organisations. This status may have been supported by the necessity for anyone seeking information to visit the accountants. Thus, by not disseminating the information, the accountant apparently becomes the information hub within the organisation. Potentially, a centre of power and thereby, status. The exact nature of this effect merits further examination.
7. Some researchers have suggested that MCSs have developed as a result of management's need to intensify the labour process. In the context of the three case studies examined here labour was in oversupply within the factories. Further, due to the roles of the co-operative, no action could be taken to reduce this surplus. It could be suggested that without any need to intensify the labour process there is no need to create sophisticated MCSs. This proposition could be further investigated.



## **Appendixes**



## **Appendix A**

### **The Ownership Contract of the public sector organisations in Tripoli Municipality**

#### **Article (1)**

##### **Aims of the factory**

1. The ... (company) will achieve ownership of the factory for producing ... its running and administration at the highest productivity.
2. The marketing and distribution the factory's products should be achieved directly or through possible distribution channels.
3. The factory's products should be developed and improved.
4. Management should help create more endogenous artistic and technical inventions, and nurture artistic talents and improve their productivity in this field.
5. In order to achieve its objectives the factory may carry out the following:
  - contract to buy and import spare parts and maintenance equipment necessary for production operations both from local and overseas markets;
  - contract to buy and import raw materials and any other equipment necessary for the running and production operations both from local and overseas markets;
  - acquire technical assistance and utilise some technical experts necessary for the running of the factory;
  - developing the quality and quantity of the factory production operation should be carried out;
  - all necessary acts or operations deemed necessary to preserve the factory belongings should be carried out;
  - all legal acts necessary should be conducted to achieve the factory's aims and plans.
6. The factory comes under the jurisdiction of the Ministry of Industry in the Tripoli Municipality.



## **Article (2)**

### **The factory location**

The factory and its departments shall be in the city of ... at the Municipality of Tripoli.

## **Article (3)**

### **The responsibility of the factory**

The factory's responsibilities are limited to its assets. Equally, the collective responsibility of the partners is limited accordingly, and any agreement contrary to this is invalid.

## **Article (4)**

### **The factory capital and the method of repayment**

- The factory's capital is limited to LD ... to be divided equally between the partners.
- The Capital is to be repaid to the state on monthly instalments. The first instalment will be due for payment by the end of the calendar month that follows the signing of this contract.
- The complete transfer of ownership will not be affected until all instalments are paid in full to the state.
- In order to guarantee the repayment of the monthly instalments and to secure the public money the partners shall pledge the necessary documentation to the Ministry of Industry, which will be handed back to the owners once all repayments are made.



## **Article (5)**

### **Increasing the Factory Capital**

The factory is empowered to increase its capital for the purposes of product development, creating new production lines, and this resolution should be agreed to by the majority of the factory members in the Productive Congress.

## **Article (6)**

### **Factory's Financial Year**

The factory financial year starts with the state financial year and ends with its end. The first financial year for the factory starts at the same time as its declaration and entry into the industrial register.

## **Article (7)**

### **The Factory Budget**

The factory shall adhere to the preparation of their own budget and final accounts at due dates in order to be approved by the Ministry of Industry at the Municipality after it is checked.

## **Article (8)**

### **Loans**

The factory is allowed to borrow from local Banks with the approval of all partners/workers/shareholders.



## **Article (9)**

### **Acceptance of new partners**

With the approval of all members/employees/shareholders, the factory can accept new members on the condition that the total number of the factory's members does not exceed the number endorsed by the Ministry of Industry at the municipality. In the employment register and on the partnership, the new member has shares of the capital as determined by Article (6) of this contract, which is due for payment at the time and in the manner upon which all members agree. The new member must in addition of paying his share pay extra payment on every previous year. The entrance of the new member does not cause any changes in the factory documents.

## **Article (10)**

### **Death of a member**

In the case of a member's decease the factory will continue in operation between the other members and inheritors are not allowed to seek ends which would result in the demise of the factory.

## **Article (11)**

### **Member expulsion**

The Productive Congress has the power to expel or repel the member from the factory when his presence in the factory will result in harm to the factory or lead to a disruption of its production process. The expelled member has the right of appeal to the primary court within thirty days from the date of expulsion.

## **Article (12)**

### **Determination of resigned or expelled member**

In the case of a member resigning or being expelled from the factory an account of his share in the return from the production should be prepared on the basis of the last



budget for the year in which the relationship between the member and the factory is terminated. All this must be resolved within six months following the endorsement of that budget.

### **Article (13)**

#### **The responsibility of the members and inheritors**

Members whose relationship with the factory is terminated remain liable for any obligations to the factory for the period of two years from the date of leaving or expulsion from the factory.

### **Article (14)**

#### **The member's share cannot be seized**

The member's share cannot be seized by his creditors as long as the factory is in operation. The Productive Congress approves that the shares of the member in debt are desolated and the factory continues in operation.

### **Article (15)**

#### **The duties of the Production Congress**

The factory shall form a Productive Congress from all members and forms a People's Committee composed of 3 to 5 members to be selected by direct secondment. The combining of the role of membership in the Congress Committee and the People's Committee is not allowed. The term of office in the People's Committee is limited to 5 years. The duties of the production conference are as follows:

1. setting the factory's internal policy and the execution of the general policy determined by the state;
2. selection and accountability of the People's Committee of the factory;
3. termination of People's Committee membership and the acceptance of resignation or dismissal of the People's Committee if the necessity dictated



- that and the selection of a new members according to the laws and regulations prevalent at the time;
4. the production conference resolution to be endorsed by the General People's Committee for industry in the municipality;
  5. endorsement of the budget and the final accounts;
  6. determination of the budget proposal for the coming year;
  7. determination of expelling a member or the accepting of new members.

## **Article (16)**

### **Management of the factory**

- The factory is to be managed by People's Committee composed of 3 to 5 members selected by the Productive Congress and endorsed by the Ministry of Industry.
- The term of office for the People's Committee members in the factory is five years. The membership could be terminated in the case of any of the following:
  1. loss of credibility and trust as a result of resolution by the Productive Congress Committee and endorsement by the Ministry of Industry at the municipality;
  2. determination of legal judgement, leading to criminal or dishonourable offence conviction;
  3. the acceptance of resignation or death or the end of the term of office.
- The People's Committee may delegate some of its duties to one or more of its members provided that it clearly states the limits of the delegation areas in the delegation resolution.

## **Article (17)**

### **Membership requirement of the People's Committee**

It is not permitted to select for office any one who was bounded, unfit for office, or lost civil rights as a result of legal action and the selection of such a person is invalid. A



member may ask for leave from his duties at the committee, if he has reasons to support this need. He must inform of his resignation in writing to the factory People's Committee in order for it to consider it and refer it to the Productive Congress for resolution.

## **Article (18)**

### **Duties and resolutions of the People's Committee**

- In order to be valid the Committee meeting must be composed of the majority of the members with the presence of its secretary or his deputy. Its resolution must be issued with anonymous agreement.
- Duties of the People's Committee of the factory are as follows:
  1. setting up of plans and programmes for achieving the aims of the factory;
  2. the execution of the Productive Congress Committee for the factory's resolution;
  3. the preparation of the budget projection, the general budget and the final accounts;
  4. following up of the activities of all the factory units in order to guarantee its synchronicity with its plans and programmes;
  5. taking the necessary steps to provide the factory needs of production requirements at suitable times;
  6. following up of the factory marketing programmes;
  7. issuing of internal regulations and within the directives issued for this matter;
  8. the taking of any steps necessary for the preservation of the factory;
  9. setting up of the training programmes in the factory;
  10. proposing factory development;
  11. the discharge of whatever directive of instruction issued to the factory from the Ministry of Industry at the municipality.



## **Article (19)**

### **Duties of the People's Committee members**

Members of the People's Committee must competently discharge duties assigned to them according to this contract, the current regulation in the factory, and any resolution issued by the Productive Congress according to the law of proxy requirements. Members of the People's Committee are responsible to the factory in case of any loss that might ensure due to their negligence in the discharge of their duties.

## **Article (20)**

### **Duties of the secretary of the factory People's Committee**

- Official representation of the factory to the courts or official departments or any area of interest to the factory.
- The endorsement of matters relating to administrative or financial issues and the execution of laws, regulations and directives concerning the factory.
- The issuing of warning and letters of admonition or directing letters to the negligent producers and the issue of letters of deduction, which do not exceed three days in the case of administrative misdemeanour.
- Stopping any producer from work in case of his committing misdemeanour requires his stopping from work until the matter is put in front of the Productive Congress.

## **Article (21)**

### **The factory's responsibility to its debtors**

All members are collectively responsible to the debtors for not discharging duties necessary for the protection of the factory and maintaining its integrity.



## **Article (22)**

### **Dissolution of the factory**

The factory is to be considered dissolved according to the following:

1. the end of its term, unless all partners agree to an extension;
2. the impossibility of achieving aims for which it was set to achieve;
3. the impossibility of running its affairs;
4. the squandering of two thirds of its Capital unless all members agree to the contrary;
5. the total agreement of its members to dissolve it upon repayment of all its dues and the endorsement of such an act by the Ministry of Industry at the municipality.

## **Article (23)**

### **Prohibition of discharging new operations after dissolution**

Partners are not permitted to conduct any further operations according to the Articles of this contract once the factory is dissolved, otherwise they collectively become liable for such operations.

## **Article (24)**

### **Appointment of Liquidates**

The Productive Congress alone will appoint one or more receivers to discharge duties related to the dissolution of the factory according to legal regulations and requirements. In the case that this is not possible any partner can ask the legal authorities to appoint a receiver. The authority of the factory's People's Committee is terminated by the appointment of a receiver. The authority of the Productive Congress remains in place until the liquidation has been completed.



## **Article (25)**

### **Duties of the Receivers**

Duties and responsibilities of receivers are set by the Law.

## **Article (26)**

### **Final Liquidation Accounts**

On completing the liquidation the receivers shall prepare an account to determine factory's assets and liabilities, remaining fixed capital and movable assets, and to propose how they are going to be divided between the partners in accordance with fiscal norms and financial regulations. The final account should be submitted to the party who appointed the receivers for comment and in the case of disagreement between the receivers and the Productive Congress in this regard the matter would be sent to the Courts for determination. The responsibility of the Productive Congress ends with the endorsement of the final accounts.

## **Article (27)**

### **Distribution of the factory's assets**

The factory's Assets shall be divided between the producers after settling its debts and assigning the money not yet due for payment to creditors, and after the returning of any expenses or loans which might be contracted for the benefit of the factory. Partners or producers may share the factory's money if that will not lead to a tangible loss of its value, but if that is not possible or may lead to a greater loss of its value, those assets shall be sold by general auction.



## **Article (28)**

### **Settlement of disputes concerning assets distribution**

Any dispute between partners concerning the determination of the factory's assets or the allocation of portions or the way they are distributed shall be referred to the courts for determination.

## **Article (29)**

### **Accounts books and records of the factory**

Partners are committed to retain books and records, which are required by law, and to record all information and declarations concerning the factory for the duration of the factory's life. The submission of these records should be made to any parties who have legal entitlements to receiving such records, and to be lodged at the secretariat of the Ministry of Industry at the municipality after the factory's liquidation.

## **Article (30)**

### **Postponement of the payment of ownership instalments**

In the case of unforeseen disabling circumstances, by which is meant circumstances without the control of the producers such as natural disasters or energy fluctuations or shortage of raw materials or production needs, it is possible for the factory to delay the payment of ownership instalments according to the stoppage period and according to the request made by the Productive Congress of the factory and after the acknowledgement of the reasons of stoppage by the Ministry of Industry.

## **Article (31)**

The partners/ selected ----- to arrange for and carry out legal and administrative requirements for the registration of the factory and its declaration and the said person shall declare his acceptance of this assignment according to the legal administrative regulations and current resolutions. He will lodge this contract with the Ministry of Industry at the municipality for legal procedures.



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